U S PHYSICAL THERAPY INC /NV
Form 10-K
March 12, 2013
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2012

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER 1-11151

U.S. PHYSICAL THERAPY, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

NEVADA	**76-0364866**
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	***(I.R.S. EMPLOYER IDENTIFICATION NO.)***

1300 WEST SAM HOUSTON PARKWAY SOUTH,

SUITE 300,

HOUSTON, TEXAS	**77042**
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)	***(ZIP CODE)***

REGISTRANT S TELEPHONE NUMBER, INCLUDING AREA CODE: (713) 297-7000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE EXCHANGE ACT:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $.01 par value	**New York Stock Exchange**

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE EXCHANGE ACT: NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes ¨ No þ

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	þ
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No þ

The aggregate market value of the shares of the registrant s common stock held by non-affiliates of the registrant at June 30, 2012 was $233,119,000 based on the closing sale price reported on the Nasdaq Global Select Market for the registrant s common stock on June 29, 2012, the last business day of the registrant s most recently completed second fiscal quarter. For purposes of this computation, all executive officers, directors and 5% or greater beneficial owners of the registrant were deemed to be affiliates. Such determination should not be deemed an admission that such executive officers, directors and beneficial owners are, in fact, affiliates of the registrant.

As of March 12, 2013, the number of shares outstanding of the registrant s common stock, par value $.01 per share, was: 12,068,388.

DOCUMENTS INCORPORATED BY REFERENCE

DOCUMENT	PART OF FORM 10-K
Portions of Definitive Proxy Statement for the 2013 Annual Meeting of Shareholders	PART III

Table of Contents

Table of Contents

		Page
PART I		
Item 1.	Business	3
Item 1A.	Risk Factors	14
Item 1B.	Unresolved Staff Comments	19
Item 2.	Properties	19
Item 3.	Legal Proceedings	19
Item 4.	Mine Safety Disclosures	19
PART II		
Item 5.	Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	20
Item 6.	Selected Financial Data	22
Item 7.	Management s Discussion and Analysis of Financial Condition and Results of Operations	23
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	35
Item 8.	Financial Statements and Supplementary Data	36
	Notes to Consolidated Financial Statements	43
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	64
Item 9A.	Controls and Procedures	64
Item 9B.	Other Information	65
PART III		
Item 10.	Directors, Executive Officers and Corporate Governace	66
Item 11.	Executive Compensation	66
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	66
Item 13.	Certain Relationships and Related Transactions, and Director Independence	66
Item 14.	Principal Accountant Fees and Services	66
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	67
Signatures		74

Table of Contents

FORWARD-LOOKING STATEMENTS

We make statements in this report that are considered to be forward-looking statements within the meaning given such term under Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements contain forward-looking information relating to the financial condition, results of operations, plans, objectives, future performance and business of our Company. These statements (often using words such as believes , expects , intends , plans , appear , should and similar words) involve risks and uncertainties that could cause actual r to differ materially from those we project. Included among such statements are those relating to opening new clinics, availability of personnel and the reimbursement environment. The forward-looking statements are based on our current views and assumptions and actual results could differ materially from those anticipated in such forward-looking statements as a result of certain risks, uncertainties, and factors, which include, but are not limited to:

changes in Medicare guidelines and reimbursement or failure of our clinics to maintain their Medicare certification status;

revenue and earnings expectations;

general economic conditions;

business and regulatory conditions including federal and state regulations;

changes as the result of government enacted national healthcare reform;

availability and cost of qualified physical therapists;

personnel productivity;

competitive, economic or reimbursement conditions in our markets which may require us to reorganize or close certain clinics and thereby incur losses and/or closure costs including the possible write-down or write-off of goodwill and other intangible assets;

changes in reimbursement rates or payment methods from third party payors including government agencies and deductibles and co-pays owed by patients;

maintaining adequate internal controls;

availability, terms, and use of capital;

acquisitions and the successful integration of the operations of the acquired businesses; and

weather and other seasonal factors.

Many factors are beyond our control. Given these uncertainties, you should not place undue reliance on our forward-looking statements. Please see the other sections of this report and our other periodic reports filed with the Securities and Exchange Commission (the SEC) for more information on these factors. Our forward-looking statements represent our estimates and assumptions only as of the date of this report. Except as required by law, we are under no obligation to update any forward-looking statement, regardless of the reason the statement is no longer accurate.

Table of Contents

PART I

ITEM 1. ***BUSINESS.***

GENERAL

Our company, U.S. Physical Therapy, Inc. (the Company), through its subsidiaries, operates outpatient physical therapy clinics that provide pre-and post-operative care and treatment for orthopedic-related disorders, sports-related injuries, preventative care, rehabilitation of injured workers and neurological-related injuries. In addition, we operate one clinic which specializes in the outpatient, non-surgical treatment of osteo arthritis degenerative joint disease and other musculoskeletal conditions (Physician Services) and perform certain services on behalf of third parties that provide physical therapy services. We primarily operate through subsidiary clinic partnerships in which we generally own a 1% general partnership interest and a 64% limited partnership interest and the managing therapist(s) of the clinics owns the remaining limited partnership interest in the majority of the clinics (hereinafter referred to as Clinic Partnerships). To a lesser extent, we operate some clinics through wholly-owned subsidiaries under profit sharing arrangements with therapists (hereinafter referred to as Wholly-Owned Facilities). Unless the context otherwise requires, references in this Annual Report on Form 10-K to we , our or us includes the Company and all of its subsidiaries.

Our strategy is to develop outpatient physical therapy clinics and acquire single and multi-clinic outpatient physical therapy practices on a national basis. At December 31, 2012, we operated 431 clinics, inclusive of one clinic that perform Physician Services (the Physician Services Clinic), in 43 states. The average age of the 431 clinics in operation at December 31, 2012 was 8.7 years. There were 329 clinics operated under Clinic Partnerships and 102 were operated as Wholly-Owned Facilities. Of the 431 clinics, we developed 294 and acquired 137. Our highest concentration of clinics are in the following states Tennessee, Texas, Michigan, Maryland, Washington, New Jersey, Wisconsin, Georgia, Arizona, Virginia, Indiana, Florida and Maine. In addition to our 431 clinics, at December 31, 2012, we also managed 15 physical therapy practices for third parties, primarily physicians.

During the last three years, we completed the following multi-clinic acquisitions:

Acquisition	Date	% Interest Acquired	Number of Clinics
	2012		
May 2012 Acquisition	May 22	70%	7
	2011		
July 2011 Acquisition	July 25	51%	20
	2010		
February 2010 Acquisition	February 26	70%	5
December 21, 2010 Acquisition	December 21	70%	6
December 31, 2010 Acquisition	December 31	65%	14

In addition to the 7 clinics in the May 2012 Acquisition, in 2012, we acquired 7 clinic practices in 7 separate transactions. Two of the acquired clinic practices operate in two new partnerships and the remaining 5 operate as satellites of existing partnerships. In 2010, we acquired two clinic practices in separate transactions. Both practices were consolidated into existing Company clinics.

We continue to seek to attract physical therapists who have established relationships with physicians and other referral sources by offering therapists a competitive salary and a share of the profits or an ownership interest in the clinic operated by that therapist. In addition, we have developed satellite clinic facilities of existing clinics, with the result that a substantial number of clinic groups operate more than one clinic location. In 2013,

Table of Contents

we intend to continue to focus on developing new clinics and on opening satellite clinics where appropriate along with increasing our patient volume through marketing and new programs. In addition, we expect to continue to acquire clinic practices.

Therapists at our clinics initially perform a comprehensive evaluation of each patient, which is then followed by a treatment plan specific to the injury as prescribed by the patient s physician. The treatment plan may include a number of procedures, including therapeutic exercise, manual therapy techniques, ultrasound, electrical stimulation, hot packs, iontophoresis, education on management of daily life skills and home exercise programs. A clinic s business primarily comes from referrals by local physicians. The principal sources of payment for the clinics services are managed care programs, commercial health insurance, Medicare/Medicaid and workers compensation insurance.

Our Company was re-incorporated in April 1992 under the laws of the State of Nevada and has operating subsidiaries organized in various states in the form of limited partnerships and wholly-owned corporations. This description of our business should be read in conjunction with our financial statements and the related notes contained elsewhere in this Annual Report on Form 10-K. Our principal executive offices are located at 1300 West Sam Houston Parkway South, Suite 300, Houston, Texas 77042. Our telephone number is (713) 297-7000. Our website is www.usph.com.

OUR CLINICS

Most of our clinics are Clinic Partnerships in which we own the general partnership interest and a majority of the limited partnership interests. The managing healthcare practitioner of the clinics usually owns a portion of the limited partnership interests. Generally, the therapist partners have no interest in the net losses of Clinic Partnerships, except to the extent of their capital accounts. Since we also develop satellite clinic facilities of existing clinics, Clinic Partnerships may consist of more than one clinic location. As of December 31, 2012, through wholly-owned subsidiaries, we owned a 1% general partnership interest in all the Clinic Partnerships, except for one partnership in which we own a 6% general partnership interest. Our limited partnership interests range from 49% to 99% in the Clinic Partnerships, but with respect to the majority of our Clinic Partnerships, we own a limited partnership interest of 64%. For the vast majority of the Clinic Partnerships, the managing healthcare practitioner is a physical therapist who owns the remaining limited partnership interest in the Clinic Partnership.

In the majority of the Clinic Partnership agreements, the therapist partner begins with a 20% interest in their Clinic Partnership earnings which increases by 3% at the end of each year thereafter up to a maximum interest of 35%.

Typically each therapist partner or director enters into an employment agreement for a term of up to three years with their Clinic Partnership. Each agreement typically provides for a covenant not to compete during the period of his or her employment and for up to two years thereafter. Under each employment agreement, the therapist partner receives a base salary and may receive a bonus based on the net revenues or profits generated by their Clinic Partnership. In the case of Clinic Partnerships, the therapist partner receives earnings distributions based upon their ownership interest. Upon termination of employment, the Company typically has the right, but is not obligated, to purchase the therapist s partnership interest in Clinic Partnerships. In connection with several of our acquired clinics, in the event that a limited minority partner s employment ceases at any time after three years from the acquisition date, we have agreed to repurchase that individual s noncontrolling interest at a predetermined multiple of earnings before interest and taxes.

Each Clinic Partnership maintains an independent local identity, while at the same time enjoying the benefits of national purchasing, negotiated third-party payor contracts, centralized support services and management practices. Under a management agreement, one of our subsidiaries provides a variety of support services to each clinic, including supervision of site selection, construction, clinic design and equipment

Table of Contents

selection, establishment of accounting systems and billing procedures and training of office support personnel, processing of accounts payable, operational direction, auditing of regulatory compliance, payroll, benefits administration, accounting services, quality assurance and marketing support.

Our typical clinic occupies approximately 1,500 to 3,000 square feet of leased space in an office building or shopping center. We attempt to lease ground level space for patient ease of access to our clinics. We also attempt to make the decor in our clinics less institutional and more aesthetically pleasing than traditional hospital clinics. Typical minimum staff at a clinic consists of a licensed physical therapist and an office manager, as well as, if appropriate, a medical advisor. As patient visits grow, staffing may also include additional physical therapists, occupational therapists, therapy assistants, aides, exercise physiologists, athletic trainers and office personnel. Therapy services are performed under the supervision of a licensed therapist.

We provide services at our clinics on an outpatient basis. Patients are usually treated for approximately one hour per day, two to three times a week, typically for two to six weeks. We generally charge for treatment on a per procedure basis. Medicare patients are charged based on prescribed time increments and Medicare billing standards. In addition, our clinics will develop, when appropriate, individual maintenance and self-management exercise programs to be continued after treatment. We continually assess the potential for developing new services and expanding the methods of providing our existing services in the most efficient manner while providing high quality patient care.

FACTORS INFLUENCING DEMAND FOR THERAPY SERVICES

We believe that the following factors, among others, influence the growth of outpatient physical therapy services:

Economic Benefits of Therapy Services. Purchasers and providers of healthcare services, such as insurance companies, health maintenance organizations, businesses and industries, continuously seek cost savings for traditional healthcare services. We believe that our therapy services provide a cost-effective way to prevent short-term disabilities from becoming chronic conditions and to speed recovery from surgery and musculoskeletal injuries.

Earlier Hospital Discharge. Changes in health insurance reimbursement, both public and private, have encouraged the earlier discharge of patients to reduce costs. We believe that early hospital discharge practices foster greater demand for outpatient physical therapy services.

Aging Population. In general, the elderly population has a greater incidence of disability compared to the population as a whole. As this segment of the population grows, we believe that demand for rehabilitation services will expand.

MARKETING

We focus our marketing efforts primarily on physicians, including orthopedic surgeons, neurosurgeons, physiatrists, internal medicine physicians, podiatrists, occupational medicine physicians and general practitioners. In marketing to the physician community, we emphasize our commitment to quality patient care and regular communication with physicians regarding patient progress. We employ personnel to assist clinic directors in developing and implementing marketing plans for the physician community and to assist in establishing relationships with health maintenance organizations, preferred provider organizations, industry and case managers and insurance companies.

SOURCES OF REVENUE

Payor sources for clinic services are primarily managed care programs, commercial health insurance, Medicare/Medicaid and workers compensation insurance. Commercial health insurance, Medicare and managed care programs generally provide coverage to patients utilizing our clinics after payment by the patients of normal

Table of Contents

deductibles and co-insurance payments. Workers compensation laws generally require employers to provide, directly or indirectly through insurance, costs of medical rehabilitation for their employees from work-related injuries and disabilities and, in some jurisdictions, mandatory vocational rehabilitation, usually without any deductibles, co-payments or cost sharing. Treatments for patients who are parties to personal injury cases are generally paid from the proceeds of settlements with insurance companies or from favorable judgments. If an unfavorable judgment is received, collection efforts are generally not pursued against the patient and the patient s account is written-off against established reserves. Bad debt reserves relating to all receivable types are regularly reviewed and adjusted as appropriate.

The following table shows our payor mix for the years ended:

	December 31, 2012		December 31, 2011		December 31, 2010	
Payor	Net Patient Revenue	Percentage	Net Patient Revenue	Percentage	Net Patient Revenue	Percentage
	(Net Patient Revenues in Thousands)					
Managed Care Program	$ 73,348	30.0%	$ 66,025	29.1%	$ 63,993	31.4%
Commercial Health Insurance	57,146	23.4%	52,697	23.3%	50,243	24.6%
Medicare/Medicaid	58,813	24.1%	56,287	24.8%	46,165	22.6%
Workers Compensation Insurance	42,144	17.2%	39,338	17.4%	34,185	16.7%
Other	12,992	5.3%	12,232	5.4%	9,523	4.7%
Total	$ 244,443	100.0%	$ 226,579	100.0%	$ 204,109	100.0%

Our business depends to a significant extent on our relationships with commercial health insurers, health maintenance organizations, preferred provider organizations and workers compensation insurers. In some geographical areas, our clinics must be approved as providers by key health maintenance organizations and preferred provider plans to obtain payments. Failure to obtain or maintain these approvals would adversely affect financial results.

During the year ended December 31, 2012, approximately 25.0% of our visits and 22.5% of our net patient revenues were from patients with Medicare program coverage. To receive Medicare reimbursement, a facility (Medicare Certified Rehabilitation Agency) or the individual therapist (Physical/Occupational Therapist in Private Practice) must meet applicable participation conditions set by the Department of Health and Human Services (HHS) relating to the type of facility, equipment, record keeping, personnel and standards of medical care, and also must comply with all state and local laws. HHS, through Centers for Medicare & Medicaid Services (CMS) and designated agencies, periodically inspects or surveys clinics/providers for approval and/or compliance. We anticipate that our newly developed clinics will generally become certified as Medicare providers or will be enrolled as a group of physical/occupation therapists in a private practice. However, we cannot assure you that newly developed clinics will be successful in becoming eligible as Medicare providers.

The Medicare program reimburses outpatient rehabilitation providers based on the Medicare Physician Fee Schedule (MPFS). The MPFS rates are automatically updated annually based on a formula, called the sustainable growth rate (SGR) formula. The use of the SGR formula has resulted in calculated automatic reductions in rates in every year since 2002; however, for each year through 2013, CMS or Congress has taken action to prevent the implementation of SGR formula reductions. For 2012, the Temporary Payroll Tax Cut Continuation Act of 2011 (TPTC) delayed application of the SGR for the first two months of the year and the Middle Class Tax Relief and Job Creation Act of 2012 (MCTRA) included a measure freezing payment rates at their then current level through December 31, 2012. The American Taxpayer Relief Act of 2012 essentially froze the Medicare physician fee schedule rates at 2012 levels through December 31, 2013, averting a scheduled 26.5% cut as a result of the SGR formula that would have taken effect on January 1, 2013. A reduction in the Medicare physician fee schedule payment rates will occur on January 1, 2014, unless Congress again takes legislative action to prevent the SGR formula reductions from going into effect.

Table of Contents

The Budget Control Act of 2011 increased the federal debt ceiling in connection with deficit reductions over the next ten years, and requires automatic reductions in federal spending by approximately $1.2 trillion. Payments to Medicare providers are subject to these automatic spending reductions, subject to a 2% cap. The American Taxpayer Relief Act of 2012 temporarily delayed the automatic, across-the-board sequestration cuts in federal spending imposed by the Budget Control Act of 2011. Unless further legislation is enacted, it is likely that there will be a 2% reduction to Medicare payments for services furnished on or after April 1, 2013.

The MCTRA directed CMS to implement a claims-based data collection program to gather additional data on patient function during the course of therapy in order to better understand patient conditions and outcomes. All practice settings that provide outpatient therapy services would be required to include this data on the claim form. Beginning on July 1, 2013, therapists will be required to report new codes and modifiers on the claim form that reflect a patient s functional limitations and goals at initial evaluation, periodically throughout care, and at discharge. For claims submitted after July 1, 2013, CMS will reject claims if the required data is not included in the claim.

As a result of the Balanced Budget Act of 1997, the formula for determining the total amount paid by Medicare in any one year for outpatient physical therapy, occupational therapy, and/or speech-language pathology services provided to any Medicare beneficiary (*i.e.*, the Therapy Cap or Limit) was established. Based on the statutory definitions which constrained how the Therapy Cap would be applied, there is one Limit for Physical Therapy and Speech Language Pathology Services combined, and one Limit for Occupational Therapy. During 2012, the annual Limit on outpatient therapy services was $1,880 for physical therapy and speech language pathology services combined and $1,880 for occupational therapy services. Pursuant to the final MPFS rule for 2013, effective January 1, 2013 the annual Limit on outpatient therapy services is $1,900 for physical therapy and speech language pathology services combined and $1,900 for occupational therapy services. Historically, these Therapy Caps applied to outpatient therapy services provided in all settings, except for services provided in departments of hospitals. However, the American Taxpayer Relief Act of 2012 extended the annual limits on therapy expenses to services furnished in hospital outpatient department settings from October 1, 2012 through December 31, 2013. Unless Congress enacts legislation to extend the application of these limits to therapy provided in hospital outpatient settings, the Therapy Caps will no longer apply to such services starting as of January 1, 2014.

In the Deficit Reduction Act of 2005, Congress implemented an exceptions process to the annual Limit for therapy expenses. Under this process, a Medicare enrollee (or person acting on behalf of the Medicare enrollee) is able to request an exception from the Therapy Caps if the provision of therapy services was deemed to be medically necessary. Therapy Cap exceptions have been available automatically for certain conditions and on a case-by-case basis upon submission of documentation of medical necessity. The MCTRA extended the exceptions process for outpatient Therapy Caps through December 31, 2012. The American Taxpayer Relief Act of 2012 extended the exceptions process for outpatient Therapy Caps through December 31, 2013. Unless Congress extends the exceptions process, the Therapy Caps will apply to all outpatient therapy services beginning January 1, 2014, except those services furnished and billed by outpatient hospital departments.

Furthermore, under the MCTRA, starting on October 1, 2012, patients who meet or exceed $3,700 in therapy expenditures during a calendar year are subject to a manual medical review prior to payment. The $3,700 threshold is applied to the combined physical therapy/speech language pathology cap; a separate $3,700 threshold is applied to the occupational therapy cap. The American Taxpayer Relief Act of 2012 extends through December 31, 2013 the requirement that Medicare perform manual medical review of therapy services beyond the $3,700 threshold and continued the process by which providers may seek pre-approval for services to be performed beyond such dollar threshold. In February 2013, CMS advised providers that the pre-approval process for services beyond the $3,700 threshold will no longer be in effect, so that all such services during the calendar year that are over the dollar threshold will be subject to a manual medical review.

CMS adopted a multiple procedure payment reduction (MPPR) for therapy services in the final update to the MPFS for calendar year 2011. During 2011, the MPPR applied to all outpatient therapy services paid under

Table of Contents

Medicare Part B occupational therapy, physical therapy and speech-language pathology. Under the policy, the Medicare program pays 100% of the practice expense component of the Relative Value Unit (RVU) for the therapy procedure with the highest practice expense RVU, then reduces the payment for the practice expense component for the second and subsequent therapy procedures or units of service furnished during the same day for the same patient, regardless of whether those therapy services are furnished in separate sessions. In 2011 and 2012 the second and subsequent therapy service furnished during the same day for the same patient was reduced by 20% in office and other non-institutional settings and by 25% in institutional settings. The American Taxpayer Relief Act of 2012 increases the payment reduction to 50%, on subsequent therapy procedures in either setting, effective April 1, 2013. This reduction in payment for our services provided to Medicare beneficiaries will negatively impact our financial results, estimated to represent an 8% to 10% reduction in overall reimbursement for services we provide to Medicare beneficiaries.

Statutes, regulations, and payment rules governing the delivery of therapy services to Medicare beneficiaries are complex and subject to interpretation. We believe that we are in compliance in all material respects with all applicable laws and regulations and are not aware of any pending or threatened investigations involving allegations of potential wrongdoing that would have a material effect on the Company s financial statements as of December 31, 2012. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare program.

Medicare regulations require that a physician or non-physician practitioner certify the need for skilled therapy services for each patient and that these services be provided under an established plan of treatment, which is periodically revised.

Medicaid has not been a material payor for us, constituting less than 2% of historical revenue.

REGULATION AND HEALTHCARE REFORM

Numerous federal, state and local regulations regulate healthcare services and those who provide them. Some states into which we may expand have laws requiring facilities employing health professionals and providing health-related services to be licensed and, in some cases, to obtain a certificate of need (that is, demonstrating to a state regulatory authority the need for, and financial feasibility of, new facilities or the commencement of new healthcare services). Only one of the states in which we currently operate requires a certificate of need for the operation of our physical therapy business functions. Our therapists and/or clinics, however, are required to be licensed, as determined by the state in which they provide services. Failure to obtain or maintain any required certificates, approvals or licenses could have a material adverse effect on our business, financial condition and results of operations.

Regulations Controlling Fraud and Abuse. Various federal and state laws regulate financial relationships involving providers of healthcare services. These laws include Section 1128B(b) of the Social Security Act (42 U.S. C. § 1320a-7b[b]) (the Fraud and Abuse Law), under which civil and criminal penalties can be imposed upon persons who, among other things, offer, solicit, pay or receive remuneration in return for (i) the referral of patients for the rendering of any item or service for which payment may be made, in whole or in part, by a Federal health care program (including Medicare and Medicaid); or (ii) purchasing, leasing, ordering, or arranging for or recommending purchasing, leasing, ordering any good, facility, service, or item for which payment may be made, in whole or in part, by a Federal health care program (including Medicare and Medicaid). We believe that our business procedures and business arrangements are in compliance with these provisions. However, the provisions are broadly written and the full extent of their specific application to specific facts and arrangements to which the Company is a party is uncertain and difficult to predict. In addition, several states have enacted state laws similar to the Fraud and Abuse Law, which may be more restrictive than the federal Fraud and Abuse Law.

Table of Contents

In 1991, the Office of the Inspector General (OIG) of the HHS issued the first of its regulations describing compensation financial arrangements that fall within a Safe Harbor and, therefore, are not viewed as illegal remuneration under the Fraud and Abuse Law. Failure to fall within a Safe Harbor does not mean that the Fraud and Abuse Law has been violated; however, the OIG has indicated that failure to fall within a Safe Harbor may subject an arrangement to increased scrutiny under a facts and circumstances test.

Our business of managing physician-owned physical therapy facilities is regulated by the Fraud and Abuse Law. However, the manner in which we contract with such facilities often falls outside the complete scope of available Safe Harbors. We believe our arrangements comply with the Fraud and Abuse Law, even though federal courts provide limited guidance as to the application of the Fraud and Abuse Law to these arrangements. If our management contracts are held to violate the Fraud and Abuse Law, it could have an adverse effect on our business, financial condition and results of operations.

In February 2000, the OIG issued a special fraud alert regarding the rental of space in physician offices by persons or entities to which the physicians refer patients. The OIG s stated concern in these arrangements is that rental payments may be disguised kickbacks to the physician-landlords to induce referrals. We rent clinic space for a few of our clinics from referring physicians and have taken the steps that we believe are necessary to ensure that all leases comply to the extent possible and applicable with the space rental Safe Harbor to the Fraud and Abuse Law.

In April 2003, the OIG issued a special advisory bulletin addressing certain complex contractual arrangements for the provision of items and services that were previously identified as suspect in a 1989 special fraud alert. This special advisory bulletin identified several characteristics commonly exhibited by suspect arrangements, the existence of one or more of which could indicate a prohibited arrangement to the OIG. Generally, the indicia of a suspect contractual joint venture as identified by the special advisory bulletin and the associated OIG advisory opinion include the following:

New Line of Business. A provider in one line of business (Owner) expands into a new line of business that can be provided to the Owner s existing patients, with another party who currently provides the same or similar item or service as the new business (Manager/Supplier).

Captive Referral Base. The arrangement predominantly or exclusively serves the Owner s existing patient base (or patients under the control or influence of the Owner).

Little or No Bona Fide Business Risk. The Owner s primary contribution to the venture is referrals; it makes little or no financial or other investment in the business, delegating the entire operation to the Manager/Supplier, while retaining profits generated from its captive referral base.

Status of the Manager/Supplier. The Manager/Supplier is a would-be competitor of the Owner s new line of business and would normally compete for the captive referrals. It has the capacity to provide virtually identical services in its own right and bill insurers and patients for them in its own name.

Scope of Services Provided by the Manager/Supplier. The Manager/Supplier provides all, or many, of the new business key services.

Remuneration. The practical effect of the arrangement, viewed in its entirety, is to provide the Owner the opportunity to bill insurers and patients for business otherwise provided by the Manager/Supplier. The remuneration from the venture to the Owner (i.e., the profits of the venture) takes into account the value and volume of business the Owner generates.

Exclusivity. The arrangement bars the Owner from providing items or services to any patients other than those coming from Owner and/or bars the Manager/Supplier from providing services in its own right to the Owner s patients.

Due to the nature of our business operations, many of our management service arrangements exhibit one or more of these characteristics. However, the Company believes it has taken steps regarding the structure of such arrangements as necessary to sufficiently distinguish them from these suspect ventures, and to comply with the

Table of Contents

requirements of the Fraud and Abuse Law. However, if the OIG believes the Company has entered into a prohibited contractual joint venture, it could have an adverse effect on our business, financial condition and results of operations.

Stark Law. Provisions of the Omnibus Budget Reconciliation Act of 1993 (42 U.S.C. § 1395nn) (the Stark Law) prohibit referrals by a physician of designated health services which are payable, in whole or in part, by Medicare or Medicaid, to an entity in which the physician or the physician s immediate family member has an investment interest or other financial relationship, subject to several exceptions. Unlike the Fraud and Abuse Law, the Stark Law is a strict liability statute. Proof of intent to violate the Stark Law is not required. Physical therapy services are among the designated health services . Further, the Stark Law has application to the Company s management contracts with individual physicians and physician groups, as well as, any other financial relationship between us and referring physicians, including any financial transaction resulting from a clinic acquisition. The Stark Law also prohibits billing for services rendered pursuant to a prohibited referral. Several states have enacted laws similar to the Stark Law. These state laws may cover all (not just Medicare and Medicaid) patients. Many federal healthcare reform proposals in the past few years have attempted to expand the Stark Law to cover all patients as well. As with the Fraud and Abuse Law, we consider the Stark Law in planning our clinics, marketing and other activities, and believe that our operations are in compliance with the Stark Law. If we violate the Stark Law, our financial results and operations could be adversely affected. Penalties for violations include denial of payment for the services, significant civil monetary penalties, and exclusion from the Medicare and Medicaid programs.

HIPAA. In an effort to further combat healthcare fraud and protect patient confidentially, Congress included several anti-fraud measures in the Health Insurance Portability and Accountability Act of 1996 (HIPAA). HIPAA created a source of funding for fraud control to coordinate federal, state and local healthcare law enforcement programs, conduct investigations, provide guidance to the healthcare industry concerning fraudulent healthcare practices, and establish a national data bank to receive and report final adverse actions. HIPAA also criminalized certain forms of health fraud against all public and private payors. Additionally, HIPAA mandates the adoption of standards regarding the exchange of healthcare information in an effort to ensure the privacy and electronic security of patient information and standards relating to the privacy of health information. Sanctions for failing to comply with HIPAA include criminal penalties and civil sanctions. In February of 2009, the American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law. Title XIII of ARRA, the Health Information Technology for Economic and Clinical Health Act (HITECH), provided for substantial Medicare and Medicaid incentives for providers to adopt electronic health records (EHRs) and grants for the development of health information exchange (HIE). Recognizing that HIE and EHR systems will not be implemented unless the public can be assured that the privacy and security of patient information in such systems is protected, HITECH also significantly expanded the scope of the privacy and security requirements under HIPAA. Most notable are the new mandatory breach notification requirements and a heightened enforcement scheme that includes increased penalties, and which now apply to business associates as well as to covered entities. In addition to HIPAA, a number of states have adopted laws and/or regulations applicable in the use and disclosure of individually identifiable health information that can be more stringent than comparable provisions under HIPAA.

We believe that our operations fully comply with applicable standards for privacy and security of protected healthcare information. We cannot predict what negative effect, if any, HIPAA/HITECH or any applicable state law or regulation will have on our business.

Other Regulatory Factors. Political, economic and regulatory influences are fundamentally changing the healthcare industry in the United States. Congress, state legislatures and the private sector continue to review and assess alternative healthcare delivery and payment systems. Potential alternative approaches could include mandated basic healthcare benefits, controls on healthcare spending through limitations on the growth of private health insurance premiums and Medicare and Medicaid spending, the creation of large insurance purchasing groups, and price controls. Legislative debate is expected to continue in the future and market forces are expected to demand only modest increases or reduced costs. For instance, managed care entities are demanding lower reimbursement rates from healthcare providers and, in some cases, are requiring or encouraging providers to

Table of Contents

accept capitated payments that may not allow providers to cover their full costs or realize traditional levels of profitability. We cannot reasonably predict what impact the adoption of any federal or state healthcare reform measures or future private sector reform may have on our business.

COMPETITION

The healthcare industry, including the physical therapy business, is highly competitive. The physical therapy business is highly fragmented with no company having as much as six percent of the market share nationally. We believe that our Company is the third largest national outpatient rehabilitation provider.

Competitive factors affecting our business include quality of care, cost, treatment outcomes, convenience of location, and relationships with, and ability to meet the needs of, referral and payor sources. Our clinics compete, directly or indirectly, with many types of healthcare providers including the physical therapy departments of hospitals, private therapy clinics, physician-owned therapy clinics, and chiropractors. We may face more intense competition if consolidation of the therapy industry continues.

We believe that our strategy of providing key therapists in a community with an opportunity to participate in ownership or clinic profitability provides us with a competitive advantage by helping to ensure the commitment of local management to the success of the clinic.

We also believe that our competitive position is enhanced by our strategy of locating our clinics, when possible, on the ground floor of buildings and shopping centers with nearby parking, thereby making the clinics more easily accessible to patients. We offer convenient hours. We also attempt to make the decor in our clinics less institutional and more aesthetically pleasing than traditional hospital clinics.

ENFORCEMENT ENVIRONMENT

In recent years, federal and state governments have launched several initiatives aimed at uncovering behavior that violates the federal civil and criminal laws regarding false claims and fraudulent billing and coding practices. Such laws require providers to adhere to complex reimbursement requirements regarding proper billing and coding in order to be compensated for their services by government payors. Our compliance program requires adherence to applicable law and promotes reimbursement education and training; however, a determination that our clinics billing and coding practices are false or fraudulent could have a material adverse effect on us.

We and our clinics are subject to federal and state laws prohibiting entities and individuals from knowingly and willfully making claims to Medicare, Medicaid and other governmental programs and third party payors that contain false or fraudulent information. The federal False Claims Act encourages private individuals to file suits on behalf of the government against healthcare providers such as us. As such suits are generally filed under seal with a court to allow the government adequate time to investigate and determine whether it will intervene in the action, the implicated healthcare providers often are unaware of the suit until the government has made its determination and the seal is lifted. Violations or alleged violations of such laws, and any related lawsuits, could result in (i) exclusion from participation in Medicare, Medicaid and other federal healthcare programs, or (ii) significant financial or criminal sanctions, resulting in the possibility of substantial financial penalties for small billing errors that are replicated in a large number of claims, as each individual claim could be deemed a separate violation. In addition, many states also have enacted similar statutes, which may include criminal penalties, substantial fines, and treble damages.

COMPLIANCE PROGRAM

Our Compliance Program. The ongoing success of our Company depends upon our reputation for quality service and ethical business practices. Our Company operates in a highly regulated environment with many federal, state and local laws and regulations. We take a proactive interest in understanding and complying with the laws and regulations that apply to our business.

Table of Contents

Our Board of Directors (the Board) has adopted a Code of Business Conduct and Ethics to clarify the ethical standards under which the Board and management carry out their duties. In addition, the Board has created a Corporate Compliance Sub-Committee of the Board s Audit Committee (Compliance Committee) whose purpose is to assist the Board and its Audit Committee (Audit Committee) in discharging their oversight responsibilities with respect to compliance with federal and state laws and regulations relating to healthcare.

We have issued an Ethics and Compliance Manual and created a compliance DVD, hand-outs and an on-line testing program. These tools were prepared to ensure that each clinic as well as every employee of our Company and subsidiaries has a clear understanding of our mutual commitment to high standards of professionalism, honesty, fairness and compliance with the law in conducting business. These standards are administered by our Compliance Officer (CO), who has the responsibility for the day-to-day oversight, administration and development of our compliance program. The CO, internal and external counsel, management and the Compliance Committee review our policies and procedures for our compliance program from time to time in an effort to improve operations and to ensure compliance with requirements of standards, laws and regulations and to reflect the on-going compliance focus areas which have been identified by the Compliance Committee. We also have established systems for reporting potential violations, educating our employees, monitoring and auditing compliance and handling enforcement and discipline.

Committees. Our Compliance Committee, appointed by the Board, consists of four independent directors. The Compliance Committee has general oversight of our Company s compliance with the legal and regulatory requirements regarding healthcare operations. The Compliance Committee relies on the expertise and knowledge of management, the CO and other compliance and legal personnel. The CO regularly communicates with the Chairman of the Compliance Committee. The Compliance Committee meets at least four times a year or more frequently as necessary to carry out its responsibilities and reports regularly to the Board regarding its actions and recommendations.

In addition, management has appointed a team to address our Company s compliance with HIPAA. The HIPAA team consists of a security officer and employees from our legal, information systems, finance, operations, compliance, business services and human resources departments. The team prepares assessments and makes recommendations regarding operational changes and/or new systems, if needed, to comply with HIPAA.

Each clinic certified as a Medicare Rehabilitation Agency has a formally appointed governing body composed of a member of management of the Company and the director/administrator of the clinic. The governing body retains legal responsibility for the overall conduct of the clinic. The members confer regularly and discuss, among other issues, clinic compliance with applicable laws and regulations. In addition, there are Professional Advisory Committees which serve as Infection Control Committees. These committees meet in the facilities and function as advisors.

The Company has in place a Risk Management Committee consisting of the CO, the Corporate in-house Legal Counsel and the Corporate Vice President of Administration. This committee reviews and monitors all employee and patient incident reports and provides clinic personnel with actions to be taken in response to the reports.

Reporting Violations. In order to facilitate our employees ability to report in confidence, anonymously and without retaliation any perceived improper work-related activities, accounting irregularities and other violations of our compliance program, we have set up an independent national compliance hotline. The compliance hotline is available to receive confidential reports of wrongdoing Monday through Friday (excluding holidays), 24 hours a day. The compliance hotline is staffed by experienced third party professionals trained to utilize utmost care and discretion in handling sensitive issues and confidential information. The information received is documented and forwarded timely to the CO, who, together with the Compliance Committee, has the power and resources to investigate and resolve matters of improper conduct.

Table of Contents

Educating Our Employees. We utilize numerous methods to train our employees in compliance related issues. The directors/administrators of each clinic are responsible to conduct the initial training sessions on compliance with existing employees. Training is based on our Ethics and Compliance Manual, inclusive of HIPAA information, and our compliance DVD. The directors/administrators also provide periodic refresher training for existing employees and one-on-one comprehensive training with new hires. The corporate compliance group responds to questions from clinic personnel and will conduct frequent teleconference meetings on topics as deemed necessary.

When a clinic opens, the CO provides a package of compliance materials containing manuals and detailed instructions for meeting Medicare Conditions of Participation Standards and other compliance requirements. During follow up training with the director/administrator of the clinic, the CO explains various details regarding requirements and compliance standards. The CO and the compliance staff will remain in contact with the director/administrator while the clinic is implementing compliance standards and will provide any assistance required. All new office managers receive training (including Medicare, regulatory and corporate compliance, insurance billing, charge entry and transaction posting and coding, daily, weekly and monthly accounting reports) from the training staff at the corporate office. The corporate compliance group will assist in continued compliance, including guidance to the clinic staff with regard to Medicare certifications, state survey requirements and responses to any inquiries from regulatory agencies.

Monitoring and Auditing Clinic Operational Compliance. Our Company has in place audit programs and other procedures to monitor and audit clinic operational compliance with applicable policies and procedures. We employ internal auditors who, as part of their job responsibilities, conduct periodic audits of each clinic. Most clinics are audited at least once every 18 months and additional focused audits are performed as deemed necessary. During these audits, particular attention is given to compliance with Medicare and internal policies, Federal and state laws and regulations, third party payor requirements, and patient chart documentation, billing, reporting, record keeping, collections and contract procedures. The audits are conducted on site and include interviews with the employees involved in management, operations, billing and accounts receivable. Formal audit reports are prepared and reviewed with corporate management and the Compliance Committee. Each clinic director/administrator receives a letter instructing them of any corrective measures required. Each clinic director/administrator then works with the compliance team and operations to ensure such corrective measures are achieved.

Handling Enforcement and Discipline. It is our policy that any employee who fails to comply with compliance program requirements or who negligently or deliberately fails to comply with known laws or regulations specifically addressed in our compliance program should be subject to disciplinary action up to and including discharge from employment. The Compliance Committee, compliance staff, human resources staff and management investigate violations of our compliance program and impose disciplinary action as considered appropriate.

EMPLOYEES

At December 31, 2012, we employed 2,677 people, of which 2,073 were full-time employees. At that date, no Company employees were governed by collective bargaining agreements or were members of a union. We consider our relations with our employees to be good.

In the states in which our current clinics are located, persons performing designated physical therapy services are required to be licensed by the state. Based on standard employee screening systems in place, all persons currently employed by us who are required to be licensed are licensed. We are not aware of any federal licensing requirements applicable to our employees.

AVAILABLE INFORMATION

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are made available free of charge on our internet website at www.usph.com as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

Table of Contents

ITEM 1A. ***RISK FACTORS.***

Our business, operations and financial condition are subject to various risks. Some of these risks are described below, and readers of this Annual Report on Form 10-K should take such risks into account in evaluating our Company or making any decision to invest in us. This section does not describe all risks applicable to our Company, our industry or our business, and it is intended only as a summary of material factors affecting our business.

Risks related to our business and operations

Our operations are subject to extensive regulation.

The healthcare industry is subject to extensive federal, state and local laws and regulations relating to:

facility and professional licensure/permits, including certificates of need;

conduct of operations, including financial relationships among healthcare providers, Medicare fraud and abuse, and physician self-referral;

addition of facilities and services; and

billing and payment for services.

In recent years, there have been heightened coordinated civil and criminal enforcement efforts by both federal and state government agencies relating to the healthcare industry. We believe we are in substantial compliance with all laws, but differing interpretations or enforcement of these laws and regulations could subject our current practices to allegations of impropriety or illegality or could require us to make changes in our methods of operations, facilities, equipment, personnel, services and capital expenditure programs and increase our operating expenses. If we fail to comply with these extensive laws and government regulations, we could become ineligible to receive government program reimbursement, suffer civil or criminal penalties or be required to make significant changes to our operations. In addition, we could be forced to expend considerable resources responding to an investigation or other enforcement action under these laws or regulations. For a more complete description of certain of these laws and regulations, see Business Regulation and Healthcare Reform in Item 1.

Healthcare reform legislation may affect our business.

In recent years, many legislative proposals have been introduced or proposed in Congress and in some state legislatures that would affect major changes in the healthcare system, either nationally or at the state level. At the federal level, Congress has continued to propose or consider healthcare budgets that substantially reduce payments under the Medicare programs. See Business- Sources of Revenue in Item 1 for more information. The ultimate content, timing or effect of any healthcare reform legislation and the impact of potential legislation on us is uncertain and difficult, if not impossible to predict. That impact may be material to our business, financial condition or results of operations.

The uncertain economic conditions and the historically high unemployment rate may have material adverse impacts on our business and financial condition that we currently cannot predict.

Unemployment in the United States has remained high while business and consumer confidence is relatively low. Although it is difficult to predict with any degree of certainty the impact on our business, these factors could materially and adversely affect our business and financial condition.

Table of Contents

We depend upon reimbursement by third-party payors.

Substantially all of our revenues are derived from private and governmental third-party payors. In 2012, approximately 75.9% of our revenues were derived collectively from managed care plans, commercial health insurers, workers compensation payors, and other private pay revenue sources and approximately 24.1% of our revenues were derived from Medicare and Medicaid. Initiatives undertaken by industry and government to contain healthcare costs affect the profitability of our clinics. These payors attempt to control healthcare costs by contracting with healthcare providers to obtain services on a discounted basis. We believe that this trend will continue and may limit reimbursement for healthcare services. If insurers or managed care companies from whom we receive substantial payments were to reduce the amounts they pay for services, our profit margins may decline, or we may lose patients if we choose not to renew our contracts with these insurers at lower rates. In addition, in certain geographical areas, our clinics must be approved as providers by key health maintenance organizations and preferred provider plans. Failure to obtain or maintain these approvals would adversely affect our financial results.

In recent years, through legislative and regulatory actions, the federal government has made substantial changes to various payment systems under the Medicare program. See Business- Sources of Revenue in Item 1 for more information. President Obama signed into law comprehensive reforms to the healthcare system, including changes to Medicare reimbursement. Additional reforms or other changes to these payment systems may be proposed or adopted, either by the U.S. Congress or by CMS. If revised regulations are adopted, the availability, methods and rates of Medicare reimbursements for services of the type furnished at our facilities could change. Some of these changes and proposed changes could adversely affect our business strategy, operations and financial results.

Decreases in Medicare reimbursement rates, implementation of annual caps, and payment reductions applied to the second and subsequent therapy services will adversely affect our financial results.

Our clinics receive payments from the Medicare program under the Medicare Physician Fee Schedule. These rates are automatically updated annually based on the SGR formula, contained in legislation. The American Taxpayer Relief Act of 2012 essentially froze the Medicare physician fee schedule rates at 2012 levels through December 31, 2013, averting a scheduled 26.5% cut as a result of the SGR formula that would have taken effect on January 1, 2013. If no further legislation is passed by Congress and signed by the President, the SGR formula will likely reduce our Medicare reimbursement rates beginning January 1, 2014.

Congress has established annual caps that limit the amount that can be paid for outpatient therapy services rendered to any Medicare beneficiary. As directed by Congress in the Deficit Reduction Act of 2005, CMS implemented an exception process for therapy expenses incurred in 2006. Under this process, a Medicare enrollee was able to request an exception from the therapy caps if the provision of therapy services was deemed to be medically necessary. Therapy cap exceptions were available automatically for certain conditions and on a case-by-case basis upon submission of documentation of medical necessity. The exception process has been extended by Congress several times. The American Taxpayer Relief Act of 2012 extended the exceptions process through December 31, 2013. The exception process will expire on January 1, 2014 unless further extended by Congress. There can be no assurance that Congress will extend it further. If the exception process is not renewed, it may have an adverse impact on our financial results.

CMS adopted a multiple procedure payment reduction (MPPR) for therapy services in the final update to the Medicare physician fee schedule for calendar year 2011. During 2011, the MPPR applied to all outpatient therapy services paid under Medicare Part B occupational therapy, physical therapy and speech-language pathology. Under the policy, the Medicare program pays 100% of the practice expense component of the therapy procedure or unit of service with the highest Relative Value Unit, and then reduces the payment for the practice expense component for the second and subsequent therapy procedures or units of service furnished during the same day for the same patient, regardless of whether those therapy services are furnished in separate sessions. In 2011 and 2012 the second and subsequent therapy service furnished during the same day for the same patient was reduced by 20% in office and other non-institutional settings and by 25% in institutional settings. The American

Table of Contents

Taxpayer Relief Act of 2012 increases the payment reduction to 50% effective April 1, 2013. This reduction in payment for our services provided to Medicare beneficiaries will negatively impact our financial results, estimated to represent an 8% to 10% reduction in overall reimbursement for services we provide to Medicare beneficiaries.

Furthermore, under the MCTRA, starting on October 1, 2012, patients who meet or exceed $3,700 in therapy expenditures during a calendar year are subject to a manual medical review prior to payment. The $3,700 threshold is applied to the combined physical therapy/speech language pathology cap; a separate $3,700 threshold is applied to the occupational therapy cap. The American Taxpayer Relief Act of 2012 extends through December 31, 2013 the requirement that Medicare perform manual medical review of therapy services beyond the $3,700 threshold and continued the process by which providers may seek pre-approval for services to be performed beyond such dollar threshold. In February 2013, CMS advised providers that the pre-approval process for services beyond the $3,700 threshold will no longer be in effect, so that all such services during the calendar year that are over the dollar threshold will be subject to a manual medical review.

The Budget Control Act of 2011 increased the federal debt ceiling in connection with deficit reductions over the next ten years, and requires automatic reductions in federal spending by approximately $1.2 trillion. Payments to Medicare providers are subject to these automatic spending reductions, subject to a 2% cap. The American Taxpayer Relief Act of 2012 temporarily delayed the automatic, across-the-board sequestration cuts in federal spending imposed by the Budget Control Act of 2011. Unless further legislation is enacted, it is likely that there will be a 2% reduction to Medicare payments for services furnished on or after April 1, 2013.

As a result of increased post-payment reviews of claims we submit to Medicare for our services, we may incur additional costs and may be required to repay amounts already paid to us.

We are subject to regular post-payment inquiries, investigations and audits of the claims we submit to Medicare for payment for our services. These post-payment reviews are increasing as a result of new government cost-containment initiatives. These additional post-payment reviews may require us to incur additional costs to respond to requests for records and to pursue the reversal of payment denials, and ultimately may require us to refund amounts paid to us by Medicare that are determined to have been overpaid.

For a further description of this and other laws and regulations involving governmental reimbursements, see Business Sources of Revenue and Regulation and Healthcare Reform in Item 1.

Our facilities are subject to extensive federal and state laws and regulations relating to the privacy of individually identifiable information.

HIPAA required the HHS to adopt standards to protect the privacy and security of individually identifiable health-related information. The department released final regulations containing privacy standards in December 2000 and published revisions to the final regulations in August 2002. The privacy regulations extensively regulate the use and disclosure of individually identifiable health-related information. The regulations also provide patients with significant rights related to understanding and controlling how their health information is used or disclosed. The security regulations require healthcare providers to implement administrative, physical and technical practices to protect the security of individually identifiable health information that is maintained or transmitted electronically. HITECH, which was signed into law in February of 2009, enhanced the privacy, security and enforcement provisions of HIPAA by, among other things establishing security breach notification requirements, allowing enforcement of HIPAA by state attorneys general, and increasing penalties for HIPAA violations. Violations of HIPAA or HITECH could result in civil or criminal penalties.

In addition to HIPAA, there are numerous federal and state laws and regulations addressing patient and consumer privacy concerns, including unauthorized access or theft of personal information. State statutes and regulations vary from state to state. Lawsuits, including class actions and action by state attorneys general, directed at companies that have experienced a privacy or security breach also can occur.

Table of Contents

The Company and its clinics have established policies and procedures in an effort to ensure compliance with these privacy related requirements. However, if there is a breach, we may be subject to various penalties and damages and may be required to incur costs to mitigate the impact of the breach on affected individuals.

We depend upon the cultivation and maintenance of relationships with the physicians in our markets.

Our success is dependent upon referrals from physicians in the communities our clinics serve and our ability to maintain good relations with these physicians and other referral sources. Physicians referring patients to our clinics are free to refer their patients to other therapy providers or to their own physician owned therapy practice. If we are unable to successfully cultivate and maintain strong relationships with physicians and other referral sources, our business may decrease and our net operating revenues may decline.

We also depend upon our ability to recruit and retain experienced physical therapists.

Our revenue generation is dependent upon referrals from physicians in the communities our clinics serve, and our ability to maintain good relations with these physicians. Our therapists are the front line for generating these referrals and we are dependent on their talents and skills to successfully cultivate and maintain strong relationships with these physicians. If we cannot recruit and retain our base of experienced and clinically skilled therapists, our business may decrease and our net operating revenues may decline. Periodically, we have clinics in isolated communities that are temporarily unable to operate due to the unavailability of a therapist who satisfies our standards.

Our revenues may fluctuate due to weather.

We have a significant number of clinics in states that normally experience snow and ice during the winter months. Also, a significant number of our clinics are located in states along the Gulf Coast and Atlantic Coast which are subject to periodic winter storms, hurricanes and other severe storm systems. Periods of severe weather may cause physical damage to our facilities or prevent our staff or patients from traveling to our clinics, which may cause a decrease in our net operating revenues.

We operate in a highly competitive industry.

We encounter competition from local, regional or national entities, some of which have superior resources or other competitive advantages. Intense competition may adversely affect our business, financial condition or results of operations. For a more complete description of this competitive environment, see Business Competition in Item 1. An adverse effect on our business, financial condition or results of operations may require us to write-down goodwill.

We may incur closure costs and losses.

The competitive, economic or reimbursement conditions in our markets in which we operate may require us to reorganize or to close certain clinics. In the event a clinic is reorganized or closed, we may incur losses and closure costs. The closure costs and losses may include, but are not limited to, lease obligations, severance, and write-down or write-off of goodwill and other intangible assets.

Future acquisitions may use significant resources, may be unsuccessful and could expose us to unforeseen liabilities.

As part of our growth strategy, we intend to continue pursuing acquisitions of outpatient physical therapy clinics. Acquisitions may involve significant cash expenditures, potential debt incurrence and operational losses, dilutive issuances of equity securities and expenses that could have an adverse effect on our financial condition and results of operations. Acquisitions involve numerous risks, including:

- the difficulty and expense of integrating acquired personnel into our business;
- the diversion of management s time from existing operations;

Table of Contents

- the potential loss of key employees of acquired companies;
- the difficulty of assignment and/or procurement of managed care contractual arrangements; and
- the assumption of the liabilities and exposure to unforeseen liabilities of acquired companies, including liabilities for failure to comply with healthcare regulations.

We may not be successful in obtaining financing for acquisitions at a reasonable cost, or such financing may contain restrictive covenants that limit our operating flexibility. We also may be unable to acquire outpatient physical therapy clinics or successfully operate such clinics following the acquisition.

Certain of our internal controls, particularly as they relate to billings and cash collections, are largely decentralized at our clinic locations.

Our clinic operations are largely decentralized and certain of our internal controls, particularly the processing of billings and cash collections, occur at the clinic level. Taken as a whole, we believe our internal controls for these functions at our clinics are adequate. Our controls for billing and cash collections largely depend on compliance with our written policies and procedures and separation of functions among clinic personnel. We also maintain corporate level controls, including an audit compliance program, that are intended to mitigate and detect any potential deficiencies in internal controls at the clinic level. The effectiveness of these controls to future periods are subject to the risk that controls may become inadequate because of changes in conditions or the level of compliance with our policies and procedures deteriorates.

Risks Relating to Our Outstanding Common Stock

Our stock price could be volatile, which could cause you to lose part or all of your investment.

The stock market has from time to time experienced significant price and volume fluctuations that may be unrelated to the operating performance of particular companies. In particular, the market price of our common stock has been and may continue to be highly volatile. During 2012, our stock price ranged from a low of $18.51 per share (on January 10, 2012) to a high of $28.40 per share (on September 21, 2012). Factors, such as announcements concerning changes in revenues and earnings expectations, regulatory conditions, including federal and state regulations, and economic and other external factors, as well as period-to-period fluctuations and financial results, may have a significant effect on the market price of our common stock.

From time to time, there has been limited trading volume in our common stock. In addition, there can be no assurance that there will continue to be a trading market or that any securities research analysts will continue to provide research coverage with respect to our common stock. It is possible that such factors will adversely affect the market for our common stock.

Issuance of shares in connection with financing transactions or under stock incentive plans will dilute current stockholders.

Pursuant to our stock incentive plans, our Compensation Committee of the Board of Directors, consisting solely of independent directors, is authorized to grant stock awards to our employees, directors and consultants. Shareholders will incur dilution upon the exercise of any outstanding stock awards or the grant of any restricted stock. In addition, if we raise additional funds by issuing additional common stock, or securities convertible into or exchangeable or exercisable for common stock, further dilution to our existing stockholders will result, and new investors could have rights superior to existing stockholders.

The number of shares of our common stock eligible for future sale could adversely affect the market price of our stock.

At December 31, 2012, we had reserved approximately 76,000 shares of common stock for issuance under outstanding options and 318,000 shares for future equity grants. All of these shares of common stock are registered for sale or resale on currently effective registration statements. We may issue additional restricted

Table of Contents

securities or register additional shares of common stock under the Securities Act of 1933, as amended (the Securities Act) in the future. The issuance of a significant number of shares of common stock upon the exercise of stock options or the availability for sale, or sale, of a substantial number of the shares of common stock eligible for future sale under effective registration statements, under Rule 144 or otherwise, could adversely affect the market price of the common stock.

Provisions in our articles of incorporation and bylaws could delay or prevent a change in control of our company, even if that change would be beneficial to our stockholders.

Certain provisions of our articles of incorporation and bylaws may delay, discourage, prevent or render more difficult an attempt to obtain control of our company, whether through a tender offer, business combination, proxy contest or otherwise. These provisions include the charter authorization of blank check preferred stock and a restriction on the ability of stockholders to call a special meeting.

ITEM 1B. ***UNRESOLVED STAFF COMMENTS.***
Not Applicable.

ITEM 2. ***PROPERTIES.***
We lease the properties used for our clinics under non-cancelable operating leases with terms ranging from one to five years, with the exception of the property for one clinic which we own. We intend to lease the premises for any new clinic locations except in rare instances where leasing is not a cost-effective alternative. Our typical clinic occupies 1,500 to 3,000 square feet.

We also lease our executive offices located in Houston, Texas, under a non-cancelable operating lease expiring in April 2017. We currently occupy approximately 37,537 square feet of space (including allocations for common areas) at our executive offices.

ITEM 3. ***LEGAL PROCEEDINGS.***
We are involved in litigation and other proceedings arising in the ordinary course of business. While the ultimate outcome of lawsuits or other proceedings cannot be predicted with certainty, we do not believe the impact of existing lawsuits or other proceedings will have a material impact on our business, financial condition or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES.
Not Applicable.

Table of Contents

PART II

ITEM 5. ***MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.***

PRICE QUOTATIONS

Our common stock has traded on the New York Stock Exchange (NYSE) since August 14, 2012 under the symbol USPH. Prior to that, our common stock was traded on the Nasdaq Global Select Market under the symbol USPH . As of March 11, 2013, there were 60 holders of record of our outstanding common stock. The table below indicates the high and low sales prices of our common stock reported for the periods presented.

	2012		2011	
Quarter	High	Low	High	Low
First	$ 23.39	$ 18.51	$ 22.69	$ 18.87
Second	25.46	22.52	26.06	21.51
Third	28.40	23.75	26.23	16.58
Fourth	28.24	22.69	21.27	16.75

Prior to 2011, we had not declared or paid cash dividends or distributions on our common stock. During 2011, we paid a quarterly dividend of $0.08 per share, totaling $0.32 per share for 2011, which amounted to a total of aggregate cash payments of dividends to holders of our common stock in 2011 of approximately $3.8 million. During 2012, we paid a quarterly dividend of $0.09 per share and a special dividend in December 2012 of $0.40 per share, totaling $0.76 per share for 2012, which amounted to a total of aggregate cash payments of dividends to holders of our common stock in 2012 of approximately $9.0 million. On December 3, 2012, we amended our Credit Agreement (as described in Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources) to allow us to pay the special dividend of $0.40 per share. In 2013, our Board of Directors declared a quarterly dividend of $0.10 per share payable to shareholders of record on March 15, 2013 to be paid on March 29, 2013. We are currently restricted from paying dividends in excess of $5,000,000 in any fiscal year on our common stock under the Credit Agreement.

Table of Contents

FIVE YEAR PERFORMANCE GRAPH

Prior to August 14, 2012, our common stock traded on the NASDAQ Stock Market. On August 14, 2012, our common stock began trading on the New York Stock Exchange (NYSE). The following performance graph compares the cumulative total stockholder return of our common stock to The NYSE Composite Index and the NYSE Health Care Index for the period from December 31, 2007 through December 31, 2012. In addition, the graph compares the total stockholder return of our common stock to The Nasdaq Stock Market United States Index and The Nasdaq Stock Market Healthcare Index, our historical comparisons, for the same period. The graph assumes that $100 was invested in our common stock and the common stock of each of the companies listed on The NYSE Composite Index , The NYSE Health Care Index, The Nasdaq Stock Market United States Index and The Nasdaq Stock Market Healthcare Index on December 31, 2007 and that any dividends were reinvested.

Comparison of Five Years Cumulative Total Return For the Year Ended December 31, 2012

	12/07	12/08	12/09	12/10	12/11	12/12
U. S. Physical Therapy, Inc.	100	93	118	138	137	192
NYSE Composite	100	59	74	82	77	87
NYSE Healthcare Index	100	74	90	91	98	110
The Nasdaq Stock Market United States Index	100	61	88	104	95	124
The Nasdaq Stock Market Healthcare Index	100	73	96	116	110	132

Table of Contents

ITEM 6. ***SELECTED FINANCIAL DATA.***

The following selected financial data should be read in conjunction with the description of our critical accounting policies set forth in Management s Discussion and Analysis of Results of Operations and Financial Condition .

	For the Years Ended December 31,				
	2012	2011	2010	2009	2008
	($ in thousands, except per share data)				
Net revenues	$ 252,088	$ 237,006	$ 211,233	$ 201,409	$ 187,686
Income from continuing operations including noncontrolling interests, net of tax	$ 26,218	$ 29,783	$ 24,700	$ 19,974	$ 17,089
Net income including noncontrolling interests	$ 26,218	$ 29,783	$ 24,700	$ 19,974	$ 17,089
Net income attributable to common shareholders	$ 17,933	$ 20,974	$ 15,645	$ 11,767	$ 10,004
Per common share					
Net income attributable to common shareholders:					
Basic	$ 1.52	$ 1.78	$ 1.34	$ 1.01	$ 0.84
Diluted	$ 1.51	$ 1.75	$ 1.32	$ 1.00	$ 0.83

	On December 31,				
	2012	2011	2010	2009	2008
	($ in thousands)				
Total assets	$ 171,714	$ 163,252	$ 140,861	$ 111,429	$ 118,247
Long-term debt, less current portion	$ 17,575	$ 23,784	$ 5,750	$ 400	$ 12,412
Working capital	$ 29,015	$ 29,343	$ 25,053	$ 18,255	$ 24,108
Current ratio	2.80	2.80	2.76	2.24	2.65
Total long-term debt to total capitalization	0.13	0.20	0.05		0.15

Table of Contents

ITEM 7. ***MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.***

EXECUTIVE SUMMARY

Our Business. We operate outpatient physical therapy clinics that provide pre- and post-operative care and treatment for a variety of orthopedic-related disorders and sports-related injuries, neurologically-related injuries and rehabilitation of injured workers.

During 2012, 2011 and 2010, we completed the following multi-clinic acquisitions:

Acquisition	Date	% Interest Acquired	Number of Clinics
	2012		
May 2012 Acquisition	May 22	70%	7
	2011		
July 2011 Acquisition	July 25	51%	20
	2010		
February 2010 Acquisition	February 26	70%	5
December 21, 2010 Acquisition	December 21	70%	6
December 31, 2010 Acquisition	December 31	65%	14

In addition to the 7 clinics in the May 2012 Acquisition, in 2012, the Company acquired 7 clinic practices in 7 separate transactions. Two of the acquired clinic practices operate in two new partnerships and the remaining 5 operate as satellites of existing partnerships. In 2010, the Company acquired two clinic practices in two separate transactions. Both practices were consolidated into existing Company clinics.

The results of operations of the acquired clinics have been included in our consolidated financial statements since the date of their acquisition.

At December 31, 2012, we operated 431 clinics in 43 states, inclusive of a Physician Services Clinic. The average age of our clinics at December 31, 2012 was 8.7 years.

In addition to our owned clinics, we also manage physical therapy facilities for third parties, primarily physicians, with 15 third-party facilities under management as of December 31, 2012.

CRITICAL ACCOUNTING POLICIES

Critical accounting policies are those that have a significant impact on our results of operations and financial position involving significant estimates requiring our judgment. Our critical accounting policies are:

Revenue Recognition. Revenues are recognized in the period in which services are rendered. Net patient revenues (patient revenues less estimated contractual adjustments) are reported at the estimated net realizable amounts from insurance companies, third-party payors, patients and others for services rendered. The Company has agreements with third-party payors that provide for payments to the Company at contracted amounts different from its established rates. The allowance for estimated contractual adjustments is based on terms of payor contracts and historical collection and write-off experience.

Revenues from physician services, sold primarily through franchisee arrangements, are considered multiple deliverables training and ongoing services. Each component can be purchased separately. Revenue is recognized over the period the respective services are provided.

Table of Contents

Contractual Allowances. Contractual allowances result from the differences between the rates charged for services performed and expected reimbursements by both insurance companies and government sponsored healthcare programs for such services. Medicare regulations and the various third party payors and managed care contracts are often complex and may include multiple reimbursement mechanisms payable for the services provided in our clinics. We estimate contractual allowances based on our interpretation of the applicable regulations, payor contracts and historical calculations. Each month the Company estimates its contractual allowance for each clinic based on payor contracts and the historical collection experience of the clinic and applies an appropriate contractual allowance reserve percentage to the gross accounts receivable balances for each payor of the clinic. Based on our historical experience, calculating the contractual allowance reserve percentage at the payor level is sufficient to allow us to provide the necessary detail and accuracy with our collectibility estimates. However, the services authorized and provided and related reimbursement are subject to interpretation that could result in payments that differ from our estimates. Payor terms are periodically revised necessitating continual review and assessment of the estimates made by management. Our billing system may not capture the exact change in our contractual allowance reserve estimate from period to period. Therefore, in order to assess the accuracy of our revenues and hence our contractual allowance reserves, our management regularly compares its cash collections to corresponding net revenues measured both in the aggregate and on a clinic-by-clinic basis. In the aggregate, the historical difference between net revenues and corresponding cash collections has generally reflected a difference within approximately 1% of net revenues. Additionally, analysis of subsequent period s contractual write-offs on a payor basis reflects a difference within approximately 1% between the actual aggregate contractual reserve percentage as compared to the estimated contractual allowance reserve percentage associated with the same period end balance. As a result, we believe that a reasonable likely change in the contractual allowance reserve estimate would not be more than 1% at December 31, 2012. For purposes of demonstrating the sensitivity of this estimate on the Company s financial condition, a one percent increase or decrease in our aggregate contractual allowance reserve percentage would decrease or increase, respectively, net patient revenue by approximately $634,000 for the year ended December 31, 2012. Management believes the changes in the estimate of the contractual allowance reserve for the periods ended December 31, 2012, 2011 and 2010 have not been material to the statement of operations.

The following table sets forth information regarding our patient accounts receivable as of the dates indicated (in thousands):

	December 31,	
	2012	2011
Gross patient accounts receivable	$ 64,101	$ 70,435
Less contractual allowances	36,533	39,948
Subtotal accounts receivable	27,568	30,487
Less allowance for doubtful accounts	1,595	2,154
Net patient accounts receivable	$ 25,973	$ 28,333

The following table presents our patient accounts receivable aging by payor class as of the dates indicated (in thousands):

	December 31, 2012			December 31, 2011		
Payor	Current to 120 Days	120+ Days	Total	Current to 120 Days	120+ Days	Total
Managed Care/ Commercial Plans	$ 9,308	$ 1,648	$ 10,956	$ 10,066	$ 2,213	$ 12,279
Medicare/Medicaid	5,451	1,089	6,540	5,964	1,758	7,722
Workers Compensation*	5,425	1,027	6,452	5,475	1,198	6,673
Self-pay	878	1,307	2,185	739	1,295	2,034
Other**	793	642	1,435	996	783	1,779
Totals	$ 21,855	$ 5,713	$ 27,568	$ 23,240	$ 7,247	$ 30,487

* Workers compensation is paid by state administrators or their designated agents.

** Other includes primarily litigation claims and, to a lesser extent, vehicular insurance claims.

24

Table of Contents

Reimbursement for Medicare beneficiaries is based upon a fee schedule published by HHS. For a more complete description of our third party revenue sources, see Business Sources of Revenue in Item 1.

Allowance for Doubtful Accounts. We determine allowances for doubtful accounts based on the specific agings and payor classifications at each clinic. We review the accounts receivable aging and rely on prior experience with particular payors to determine an appropriate reserve for doubtful accounts. Historically, clinics that have a large number of aged accounts generally have less favorable collection experience, and thus, require a higher allowance. Accounts that are ultimately determined to be uncollectible are written off against our bad debt allowance. The amount of our aggregate allowance for doubtful accounts is regularly reviewed for adequacy in light of current and historical experience.

Accounting for Income Taxes. We account for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount to be recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

We do not believe that we have any significant uncertain tax positions at December 31, 2012, nor is this expected to change within the next twelve months due to the settlement and expiration of statutes of limitation.

We did not have any accrued interest or penalties associated with any unrecognized tax benefits nor was any interest expense recognized during the twelve months ended December 31, 2012 and 2011.

Carrying Value of Long-Lived Assets. Our property and equipment, intangible assets and goodwill (collectively, our long-lived assets) comprise a significant portion of our total assets. The accounting standards require that we periodically, and upon the occurrence of certain events, assess the recoverability of our long-lived assets. If the carrying value of our property and equipment exceeds their undiscounted cash flows, we are required to write the carrying value down to estimated fair value.

Goodwill. The fair value of goodwill and other intangible assets with indefinite lives are tested for impairment annually and upon the occurrence of certain events, and are written down to fair value if considered impaired. The Company evaluates goodwill for impairment on at least an annual basis (in its third quarter) by comparing the fair value of its reporting units to the carrying value of each reporting unit including related goodwill. We operate a one segment business which is made up of various clinics within partnerships. The partnerships are components of regions and are aggregated to the operating segment level for the purpose of determining our reporting units when performing our annual goodwill impairment test.

An impairment loss generally would be recognized when the carrying amount of the net assets of a reporting unit, inclusive of goodwill and other intangible assets, exceeds the estimated fair value of the reporting unit. The estimated fair value of a reporting unit is determined using two factors: (i) earnings prior to taxes, depreciation and amortization for the reporting unit multiplied by a price/earnings ratio used in the industry and (ii) a discounted cash flow analysis. A weight is assigned to each factor and the sum of each weight times the factor is considered the estimated fair value. For 2012, the factors (i.e., price/earnings ratio, discount rate and residual capitalization rate) were updated to reflect current market conditions. The evaluation of goodwill in 2012, 2011 and 2010 did not result in any goodwill amounts that were deemed impaired.

Table of Contents

SELECTED OPERATING AND FINANCIAL DATA

The following table and discussion relates to continuing operations unless otherwise noted. The defined terms with their respective description used in the following discussion are listed below:

2012	Year ended December 31, 2012
2011	Year ended December 31, 2011
2010	Year ended December 31, 2010
New Clinics	Clinics opened or acquired during the year ended December 31, 2012
Mature Clinics	Clinics opened or acquired prior to January 1, 2012
2011 New Clinics	Clinics opened or acquired during the year ended December 31, 2011
2011 Mature Clinics	Clinics opened or acquired prior to January 1, 2011
2010 New Clinics	Clinics opened or acquired during the year ended December 31, 2010
2010 Mature Clinics	Clinics opened or acquired prior to January 1, 2010

The following table presents selected operating and financial data, used by management as key indicators of our operating performance:

	For the Years Ended December 31,		
	2012	2011	2010
Number of clinics, at the end of period	431	416	392
Working Days	255	255	254
Average visits per day per clinic	21.7	20.9	20.5
Total patient visits	2,315,390	2,163,679	1,926,892
Net patient revenue per visit	$ 105.57	$ 104.72	$ 105.92

RESULTS OF OPERATIONS

FISCAL YEAR 2012 COMPARED TO FISCAL 2011

Net revenues rose 6.4 % to $252.1 million for 2012 from $237.0 million for 2011 due to increases in net patient revenues offset partially by a decrease in other revenues as discussed below. The 2012 results includes seven months of operations of the May 2012 Acquisition. The 2011 results include five months of operations of the July 2011 Acquisition.

Reported net income attributable to common shareholders for 2012 decreased 14.5% to $17.9 million from $21.0 million in 2011. Diluted earnings per share was $1.51 for 2012 and $1.75 for 2011. Included in the 2011 results is a pretax gain of $5.4 million related to a purchase price settlement on the February 2010 Acquisition that occurred beyond our purchase price measurement date. Excluding this 2011 gain, diluted earnings per share from operations would have been $1.35 for 2011. In comparison to adjusted diluted earnings per share of $1.35 for 2011, the 2012 diluted earnings per share of $1.51 represents an increase of 11.9% in 2012 from 2011. See table below (in thousands).

	Year Ended December 31,	
	2012	2011
Net income attributable to common shareholders	$ 17,933	$ 20,974
Gain on purchase price settlement of $5,434 less tax effect of $629		(4,805)
Adjusted net income attributable to common shareholders	$ 17,933	$ 16,169
Adjusted net income attributable to common shareholders per diluted share	$ 1.51	$ 1.35

Table of Contents

Net Patient Revenues

Net patient revenues increased to $244.4 million for 2012 from $226.6 million for 2011, an increase of $17.8 million, or 7.9%, primarily due to an increase in patient visits from 2.2 million to 2.3 million. The increase in net patient revenues of $17.8 million consisted of an increase of $12.2 million from Mature Clinics and $5.6 million from New Clinics. The $12.2 million from Mature Clinics is primarily due to the July 2011 Acquisition. The 2012 results include 12 months of operations of the July 2011 Acquisition and the 2011 results include five months of operations.

Total patient visits increased to 2,315,000 for 2012 from 2,164,000 for 2011. The growth in patient visits was attributable to 51,000 visits in New Clinics, primarily due to the May 2012 Acquisition, and an increase of 100,000 visits for Mature Clinics, primarily due to the July 2011 Acquisition.

Net patient revenues are based on established billing rates less allowances and discounts for patients covered by contractual programs and workers compensation. Net patient revenues reflect contractual and other adjustments, which we evaluate monthly, relating to patient discounts from certain payors. Payments received under these programs are based on predetermined rates and are generally less than the established billing rates of the clinics.

Other Revenues

Other revenues decreased by $2.8 million from $10.4 million to $7.6 million primarily due to a reduction in revenue from physician services, which include clinical services related to intra articular joint and lumbar osteoarthritis programs as well as electro-diagnostic analysis.

Clinic Operating Costs

Clinic operating costs were 75.2% of net revenues for 2012 and 74.4% of net revenues for 2011. Each component of clinic operating costs is discussed below:

Clinic Operating Costs Salaries and Related Costs

Salaries and related costs increased to $132.8 million for 2012 from $125.1 million for 2011, an increase of $7.7 million, or 6.2%. Approximately $3.7 million of the increase was attributable to New Clinics. The remaining $4.0 million of the increase was due to $5.9 million in higher costs at various 2011 New Clinics offset by a decrease of $1.9 million in costs at 2011 Mature Clinics. Salaries and related costs as a percentage of net revenues was 52.7% for 2012 and 52.8% for 2011.

Clinic Operating Costs Rent, Clinic Supplies and Other

Rent, clinic supplies and other costs increased to $51.6 million for 2012 from $47.4 million for 2011, an increase of $4.2 million, or 8.9%. For 2012, New Clinics accounted for approximately $1.7 million of the increase and 2011 New Clinics accounted for approximately $4.0 million of the increase due to a full year of activity for clinics developed or acquired in 2011. Rent, clinic supplies and other costs for 2011 Mature Clinics decreased $1.5 million in 2012 as compared to 2011 due to cost containment efforts. Rent, clinic supplies and other costs as a percent of net revenues was 20.5% for 2012 and 20.0% for 2011.

Clinic Operating Costs Provision for Doubtful Accounts

The provision for doubtful accounts for net patient receivables of $4.7 million as a percentage of net patient revenues was 1.9% for 2012 and 1.7% for 2011. During 2012, we recorded a reserve for a receivable from a management contract of $0.1 million.

Table of Contents

Our allowance for bad debts as a percentage of total patient accounts receivable was 5.8% at December 31, 2012 and 7.0% at December 31, 2011. The allowance for doubtful accounts at the end of each period is based on a detailed, clinic-by-clinic review of overdue accounts and is regularly reviewed in the aggregate in light of historical experience.

The accounts receivable days outstanding were 42 days at December 31, 2012 and 48 days at December 31, 2011. Net patient receivables in the amount of $4.9 million and $3.0 million were written-off in 2012 and 2011, respectively.

Closure Costs

For 2012, closure costs amounted to $211,000. In 2011, closure costs amounted to $59,000.

Gross Margin

In 2012, the gross margin from our core physical therapy business increased by $4.6 million, or 7.9%, as compared to 2011. The margin from the physician services business decreased by $2.7 million. See table below (in thousands).

	Year Ended December 31,	
	2012	2011
Gross margin physical therapy services	$ 62,945	$ 58,339
Gross margin physician services	(360)	2,310
Gross margin	$ 62,585	$ 60,649

Corporate Office Costs

Corporate office costs, consisting primarily of salaries, benefits and equity based compensation of corporate office personnel and directors, rent, insurance costs, depreciation and amortization, travel, legal, compliance, professional, marketing and recruiting fees, were $24.8 million for 2012 and $24.7 million for 2011. Corporate office costs were reduced as a percentage of net revenues to 9.8% for 2012 from 10.4% for 2011.

Interest and Other Income, net

Interest and other income, net for 2011 included a pretax gain of $5.4 million related to a purchase price settlement on the February 2010 Acquisition that occurred beyond our purchase price measurement date. The settlement included $1.5 million in cash, $0.1 million in debt forgiveness and $3.8 million in exchange of the remaining noncontrolling interest.

Interest Expense

Interest expense increased to $557,000 for 2012 from $496,000 for 2011 primarily due to higher average borrowings. At December 31, 2012, $17.4 million was outstanding under our revolving credit facility. See Liquidity and Capital Resources below for a discussion of the terms of our revolving credit facility.

Provision for Income Taxes

The provision for income taxes was $11.0 million for 2012 and 2011. For 2012, we accrued state and federal income taxes at an effective tax rate (provision for taxes divided by the difference between income from operations and net income attributable to noncontrolling interest) of 38.1%. In 2012, the income tax provision was reduced by $350,000 related to a taxable deduction charged to additional-paid-in-capital for the reduction of

Table of Contents

a subsidiary intercompany loan and included a charge of $162,000 for a true-up of our 2011 tax provision based on a detailed reconciliation of our federal and state taxes payable and receivable accounts along with our federal and state deferred tax asset and liability accounts. For 2011, we accrued state and federal income taxes at an effective tax rate (provision for taxes divided by the difference between income from operations and net income attributable to noncontrolling interest) of 34.6%. Of the $5.4 million gain mentioned above, $3.8 million was non taxable.

Net Income Attributable to Noncontrolling Interests

Net income attributable to noncontrolling interests was $8.3 million in 2012 compared to $8.8 million in 2011. As a percentage of operating income before corporate office costs, net income attributable to noncontrolling interests was 13.2% in 2012 compared to 14.5% in 2011. The reduction is attributable to the Company s increased ownership interest in certain physical therapy partnerships.

FISCAL YEAR 2011 COMPARED TO FISCAL 2010

Net revenues rose 12.2% to $237.0 million for 2011 from $211.2 million for 2010 due to increases in net patient revenues and other revenues as discussed below. The 2011 results include five months of operations of the July 2011 Acquisition. The 2010 results include 10 months of operations for the February 2010 Acquisition and eight days of operations for the December 21, 2010 Acquisition. The 2011 and 2010 results include 255 days and 254 days of operations, respectively.

Net income attributable to common shareholders for 2011 increased 34.1% to $21.0 million from $15.6 million in 2010. Diluted earnings per share rose to $1.75 from $1.32. Included in the 2011 results is a pretax gain of $5.4 million related to a purchase price settlement on the February 2010 Acquisition. Included in the 2010 results was a positive adjustment in the income tax provision of $0.8 million and a gain from the sale of a five clinic joint venture of approximately $0.6 million. Excluding the 2011 and 2010 gains and the 2010 tax adjustment, diluted earnings per shares from operations would have been $1.35 for 2011 and $1.22 for 2010, an increase of 10.7%. See table below

	Year Ended December 31,	
	2011	2010
	(In thousands, except per share data)	
Net income attributable to common shareholders	$ 20,974	$ 15,645
Gain on purchase price settlement of $5,434 less tax effect of $629	(4,805)	
Positive adjustment in income tax provision		(814)
Gain on the sale of a five clinic joint venture of $578 less tax effect of $227		(351)
Adjusted net income attributable to common shareholders	$ 16,169	$ 14,480
Adjusted net income attributable to common shareholders per diluted share	$ 1.35	$ 1.22

Net Patient Revenues

Net patient revenues increased to $226.6 million for 2011 from $204.1 million for 2010, an increase of $22.5 million, or 11.0%, primarily due to an increase in patient visits from 1.9 million to 2.2 million. The increase in net patient revenues of $22.5 million consisted of an increase of $14.3 million from 2011 Mature Clinics and $8.2 million from 2011 New Clinics, primarily due to the July 2011 Acquisition. The $14.4 million from 2011 Mature Clinics is made up of an increase of $14.2 million from the 2010 Acquisitions and $0.2 million from other 2011 Mature Clinics.

29

Table of Contents

Total patient visits increased to 2,164,000 for 2011 from 1,927,000 for 2010. The growth in patient visits was attributable to 76,000 visits in 2011 New Clinics, primarily due to the July 2011 Acquisition and an increase of 162,000 visits for 2011 Mature Clinics, primarily due to the 2010 Acquisitions.

Net patient revenues are based on established billing rates less allowances and discounts for patients covered by contractual programs and workers compensation. Net patient revenues reflect contractual and other adjustments, which we evaluate monthly, relating to patient discounts from certain payors. Payments received under these programs are based on predetermined rates and are generally less than the established billing rates of the clinics.

Other Revenues

Other revenues increased by $3.3 million from $7.1 million to $10.4 million primarily due to $2.5 million higher revenues from physician services, which include clinical services related to intra articular joint and lumbar osteoarthritis programs as well as electro-diagnostic analysis, and $0.5 million from a management contract acquired as part of the 2010 Acquisitions.

Clinic Operating Costs

Clinic operating costs were 74.4% of net revenues for 2011 and 73.5% of net revenues for 2010. Each component of clinic operating costs is discussed below:

Clinic Operating Costs Salaries and Related Costs

Salaries and related costs increased to $125.1 million for 2011 from $110.9 million for 2010, an increase of $14.2 million, or 12.8%. Approximately $5.5 million of the increase was attributable to 2011 New Clinics. The remaining $8.7 million of the increase was due to $10.4 million in higher costs at various 2010 New Clinics offset by a decrease of $1.7 million in costs at 2010 Mature Clinics. Salaries and related costs as a percentage of net revenues was 52.8% for 2011 and 52.5% for 2010.

Clinic Operating Costs Rent, Clinic Supplies and Other

Rent, clinic supplies and other costs increased to $47.4 million for 2011 from $40.9 million for 2010, an increase of $6.5 million, or 15.8%. For 2011, 2011 New Clinics accounted for approximately $2.8 million of the increase and 2010 New Clinics accounted for approximately $4.2 million of the increase due to a full year of activity for clinics developed or acquired in 2010. Rent, clinic supplies and other costs for 2010 Mature Clinics decreased $0.5 million in 2011 as compared to 2010 due to cost containment efforts. Rent, clinic supplies and other costs as a percent of net revenues was 20.0% for 2011 and 19.4% for 2010.

Clinic Operating Costs Provision for Doubtful Accounts

The provision for doubtful accounts for net patient receivables as a percentage of net patient revenues was 1.7% for 2011 and 1.6% for 2010. Our allowance for bad debts as a percentage of total patient accounts receivable was 7.0% at December 31, 2011 and 8.1% at December 31, 2010. The allowance for doubtful accounts at the end of each period is based on a detailed, clinic-by-clinic review of overdue accounts and is regularly reviewed in the aggregate in light of historical experience.

The accounts receivable days outstanding were 48 days at December 31, 2011 and 45 days at December 31, 2010. Receivables in the amount of $3.0 million and $2.8 million were written-off in 2011 and 2010, respectively.

Closure Costs

For 2011, closure costs amounted to $59,000 related to the closure of 17 clinics. In 2010, 15 clinics were closed with closure costs amounting to $163,000.

Table of Contents

Corporate Office Costs

Corporate office costs, consisting primarily of salaries, benefits and equity based compensation of corporate office personnel and directors, rent, insurance costs, depreciation and amortization, travel, legal, compliance, professional, marketing and recruiting fees, were $24.7 million for 2011 and $22.8 million for 2010, an increase of $1.9 million inclusive of $0.5 million related to a potential legal settlement. Corporate office costs were reduced as a percentage of net revenues to 10.4% for 2011 from 10.8% for 2010.

Interest and Other Income, net

Interest and other income for 2011 included a pretax gain of $5.4 million related to a purchase price settlement on the February 2010 Acquisition that occurred beyond our purchase price measurement date. The settlement included $1.5 million in cash, $0.1 million in debt forgiveness and $3.8 million in exchange of the remaining noncontrolling interest. Interest and other income for 2010 included a pre-tax gain of $578,000 from the sale of our 51.0% interest in a five clinic Texas joint venture.

Interest Expense

Interest expense increased to $496,000 for 2011 from $236,000 for 2010 primarily due to higher average borrowings. At December 31, 2011, $23.5 million was outstanding under our revolving credit facility. See Liquidity and Capital Resources below for a discussion of the terms of our revolving credit facility.

Provision for Income Taxes

The provision for income taxes increased to $11.1 million for 2011 from $8.8 million for 2010, an increase of approximately $2.3 million, primarily as a result of higher pre-tax income. For 2011, we accrued state and federal income taxes at an effective tax rate (provision for taxes divided by the difference between income from operations and net income attributable to noncontrolling interest) of 34.6%. Of the $5.4 million gain mentioned above, $3.8 million was non taxable. During the fourth quarter of 2010, we completed a process to perform a detailed reconciliation of our federal and state taxes payable and receivable accounts along with our federal and state deferred tax asset and liability accounts. Historically, calculations of these tax-related accounts were performed through summary estimates and analysis. As a result of this detailed analysis, we recorded a reduction in our current state income tax provision of $814,000. Without the effect of the $814,000, during 2010, we accrued state and federal income taxes at an effective tax rate of 39.4%. We performed a similar reconciliation process during the fourth quarter of 2011 which did not yield a significant adjustment.

Net Income Attributable to Noncontrolling Interests

Net income attributable to noncontrolling interests was $8.8 million in 2011 compared to $9.1 million in 2010. As a percentage of operating income before corporate office costs, net income attributable to noncontrolling interests was 14.5% in 2011 compared to 16.2% in 2010. The reduction is attributable to the Company s increased ownership interest in certain physical therapy partnerships.

LIQUIDITY AND CAPITAL RESOURCES

We believe that our business is generating sufficient cash flow from operating activities to allow us to meet our short-term and long-term cash requirements, other than those with respect to future significant acquisitions. At December 31, 2012, we had $11.7 million in cash and cash equivalents compared to $10.0 million at December 31, 2011. Although the start-up costs associated with opening new clinics and our planned capital expenditures are significant, we believe that our cash and cash equivalents and availability under our revolving credit facility are sufficient to fund the working capital needs of our operating subsidiaries, future clinic development and single practice acquisitions and investments through at least December 2013. The amount

Table of Contents

outstanding under our revolving credit facility was $17.4 million at December 31, 2012 compared to $23.5 million at December 31, 2011. At December 31, 2012, we had $57.6 million available under our revolving credit facility. Significant acquisitions would likely require financing under our revolving credit facility.

The increase in cash and cash equivalents of $1.7 million from December 31, 2011 to December 31, 2012 was due primarily to $39.3 million provided by operations and $1.4 million from the tax benefit of stock options exercised. The major uses of cash for investing and financing activities included: distributions to noncontrolling interests ($9.3 million), payments of cash dividends to our shareholders ($9.0 million), purchase of businesses ($7.9 million), net reduction of amounts outstanding under our credit facility ($6.1 million), purchases of fixed assets ($4.2 million), acquisitions of noncontrolling interests, net of sales of noncontrolling interest ($2.0 million), and payments on notes payable ($0.4 million).

Effective August 27, 2007, we entered into a credit agreement with a commitment for a $30.0 million revolving credit facility which was increased to $50.0 million effective June 4, 2008 (Credit Agreement). Effective March 18, 2009, we amended the Credit Agreement to permit us to purchase up to $15,000,000 of our common stock subject to compliance with certain covenants, including the requirement that after giving effect to any stock purchase, our consolidated leverage ratio (as defined in the Credit Agreement) be less than 1.0 to 1.0 and that any stock repurchased be retired within seven days of purchase. Effective October 13, 2010, we amended the Credit Agreement to extend the maturity date from August 31, 2011 to August 31, 2015. In addition, the Credit Agreement was amended to adjust the pricing grid which is based on our consolidated leverage ratio with the applicable spread over LIBOR ranging from 1.6% to 2.5% or the applicable spread over the Base Rate ranging from .1% to 1%. On July 14, 2011, we amended the Credit Agreement to increase the commitment from $50.0 million to $75.0 million. Effective October 24, 2012, we amended the Credit Agreement to permit us to purchase, commencing on October 24, 2012 and at all times thereafter, up to $15,000,000 of our common stock subject to compliance with covenants. On December 3, 2012, we amended the Credit Agreement to allow us to pay a special dividend of $0.40 per share. The Credit Agreement is unsecured and has loan covenants, including requirements that we comply with a consolidated fixed charge coverage ratio and consolidated leverage ratio. Proceeds from the Credit Agreement may be used for working capital, acquisitions, purchases of our common stock, dividend payments to our common stockholders, capital expenditures and other corporate purposes. Fees under the Credit Agreement include an unused commitment fee ranging from .1% to .25% depending on our consolidated leverage ratio and the amount of funds outstanding under the Credit Agreement. On December 31, 2012, $17.4 million was outstanding on the revolving credit facility resulting in $57.6 million of availability, and we were in compliance with all of the covenants thereunder.

The purchase price for the 70% interest in the May 2012 Acquisition was $6,090,000 in cash and $250,000 in seller notes, that are payable in two principal installments totaling $125,000 each, plus any accrued interest, in May 2013 and 2014. The seller notes accrue interest at 3.25% per annum. In addition to the May 2012 Acquisition, in 2012, the Company, through its subsidiaries, purchased 7 outpatient therapy practices in 7 transactions for aggregate cash consideration of $1,938,000 and, one transaction a $100,000 note payable. In addition, in 15 separate transactions during 2012, we purchased partnership interests in 15 partnerships in which we had an existing controlling interest. The interests in the partnerships purchased ranged from 10% to 35%. The aggregate of the purchase prices paid was $2.2 million, which included $0.2 million of undistributed earnings. The remaining purchase price of $2.0 million, less future tax benefits of $0.8 million, was recognized as an adjustment to additional paid-in capital. During 2012, we sold interests in the range of 0.64% to 1% in three partnerships for an aggregate price of $239,000. This amount less related undistributed earnings of $5,000 was credited to additional paid-in capital.

The purchase price for the 51% interest in the July 2011 Acquisition was $8,426,000, which consisted of $8,226,000 in cash and a $200,000 seller note, that is payable in two principal installments totaling $100,000 each, plus any accrued interest, in July 2012 and 2013. The seller note accrues interest at 3.25% per annum. In addition, in six separate transactions during 2011, we purchased a total of 22.2% of the 30% non-controlling interest in STAR Physical Therapy, LP, a subsidiary of the Company (STAR). The aggregate purchase price

Table of Contents

paid for the 22.2% interest was $16.9 million, which included $0.8 million of undistributed earnings. The remaining purchase price of $16.1 million, less future tax benefits of $6.3 million, was recognized as an adjustment to additional paid-in capital. After these transactions, we owned 92.2% and the non-controlling interest limited partners in aggregate owned the remaining 7.8% in the partnership.

Effective June 30, 2011, we purchased the 35% non-controlling interest in one of our Texas partnerships. The aggregate purchase price for the 35% interest was $3.9 million, of which $3.5 million was paid in cash and $367,272 was paid in the form of a note to the seller. The purchase price included $0.2 million of undistributed earnings and $0.2 million in invested capital. The remaining purchase price of $3.5 million, less future tax benefits of $1.4 million, was recognized as an adjustment to additional paid-in capital. After this transaction, we own 100% of the partnership.

In addition, during 2011, we purchased the non-controlling interests of several other partners for $142,000, which included $48,000 of undistributed earnings and sold an additional interest to an existing partner for $58,000. The net purchase price of approximately $36,000, less future tax benefits of $23,000, was recognized as an adjustment to additional paid-in capital.

Historically, we have generated sufficient cash from operations to fund our development activities and to cover operational needs. We plan to continue developing new clinics and making additional acquisitions in selected markets. We have from time to time purchased the noncontrolling interests of limited partners in our Clinic Partnerships. We may purchase additional noncontrolling interests in the future. Generally, any acquisition or purchase of noncontrolling interests is expected to be accomplished using a combination of cash and financing. Any large acquisition would likely require financing.

We make reasonable and appropriate efforts to collect accounts receivable, including applicable deductible and co-payment amounts. Claims are submitted to payors daily, weekly or monthly in accordance with our policy or payor s requirements. When possible, we submit our claims electronically. The collection process is time consuming and typically involves the submission of claims to multiple payors whose payment of claims may be dependent upon the payment of another payor. Claims under litigation and vehicular incidents can take a year or longer to collect. Medicare and other payor claims relating to new clinics awaiting Medicare Rehab Agency status approval initially may not be submitted for six months or more. When all reasonable internal collection efforts have been exhausted, accounts are written off prior to sending them to outside collection firms. With managed care, commercial health plans and self-pay payor type receivables, the write-off generally occurs after the account receivable has been outstanding for 120 days or longer.

We have future obligations for debt repayments, employment agreements and future minimum rentals under operating leases. The obligations as of December 31, 2012 are summarized as follows (in thousands):

Contractual Obligation	Total	2013	2014	2015	2016	2017	Thereafter
Credit Agreement and Notes Payable	$ 18,034	$ 459	$ 175	$ 17,400	$	$	$
Interest Payable	$ 27	21	6				
Employee Agreements	$ 23,317	17,387	4,315	1,195	381	39	
Operating Leases	$ 47,620	16,254	11,900	9,105	5,526	2,915	1,920
	$ 88,998	$ 34,121	$ 16,396	$ 27,700	$ 5,907	$ 2,954	$ 1,920

We generally enter into various notes payable as a means of financing our acquisitions. Our present outstanding notes payable relate only to certain of the acquisitions of businesses and noncontrolling interests that occurred in 2012 and 2011. For those acquisitions, we entered into several notes payables aggregating $0.9 million. The notes are payable in equal annual installments of principal over two years plus any accrued and unpaid interest. Interest accrues at various interest rates ranging from 3.25% to 4.0% per annum. In addition, we assumed leases with remaining terms of 1 month to 6 years for the operating facilities. At December 31, 2012, the balance on these notes payable was $0.6 million.

Table of Contents

In conjunction with the above mentioned acquisitions, in the event that a limited minority partner s employment ceases at any time after three years from the acquisition date, we have agreed to repurchase that individual s noncontrolling interest at a predetermined multiple of earnings before interest and taxes.

The purchase agreement related to an acquisition that occurred in 2008 provided for possible contingent consideration of up to $3,781,000 based on the achievement of a designated level of operating results within a three-year period following the acquisition. In 2009, 2010 and 2011, we paid $1,179,000, $1,080,000 and $1,522,000, respectively, of additional consideration related to the operating results of such acquired business. Those amounts were recorded as additional goodwill.

From September 2001 through December 31, 2008, the Board authorized us to purchase, in the open market or in privately negotiated transactions, up to 2,250,000 shares of our common stock. In March 2009, the Board authorized the repurchase of up to 10% or approximately 1,200,000 shares of our common stock (March 2009 Authorization). In connection with the March 2009 Authorization, we amended our bank credit agreement to permit the share repurchases of up to $15,000,000. We are required to retire shares purchased under the March 2009 Authorization. Effective October 24, 2012, the Credit Agreement was amended to permit us to purchase, commencing on October 24, 2012 and at all times thereafter, up to $15,000,000 of our common stock subject to compliance with covenants. Since there is no expiration date for these share repurchase programs, additional shares may be purchased from time to time in the open market or private transactions depending on price, availability and our cash position. In 2012, we did not purchase any shares under these programs. During 2011, we purchased 254,642 shares of our common stock for an aggregate cost of $4.7 million. During 2010, we purchased 86,522 shares for an aggregate purchase price of $1.4 million. There are approximately 390,000 shares remaining that could be purchased under these programs.

Off Balance Sheet Arrangements

With the exception of operating leases for our executive offices and clinic facilities discussed in Note 13 to our consolidated financial statements included in Item 8, we have no off-balance sheet debt or other off-balance sheet financing arrangements.

FACTORS AFFECTING FUTURE RESULTS

The risks related to our business and operations include:

- The uncertain economic conditions and the historically high unemployment rate in the United States may have material adverse impacts on our business and financial condition that we currently cannot predict.
- We depend upon reimbursement by third-party payors including Medicare and Medicaid.
- Changes as a result of healthcare reform legislation may affect our business.
- We depend upon the cultivation and maintenance of relationships with the physicians in our markets.
- We also depend upon our ability to recruit and retain experienced physical therapists.
- Our revenues may fluctuate due to weather.
- Our operations are subject to extensive regulation.

We operate in a highly competitive industry.

We may incur closure costs and losses.

Future acquisitions may use significant resources, may be unsuccessful and could expose us to unforeseen liabilities.

Table of Contents

Certain of our internal controls, particularly as they relate to billings and cash collections, are largely decentralized at our clinic locations.

See Risk Factors in Item 1A of this Annual Report on Form 10-K.

ITEM 7A. ***QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK***

We do not maintain any derivative instruments such as interest rate swap arrangements, hedging contracts, futures contracts or the like. Our only indebtedness as of December 31, 2012 was seller notes of $0.6 million and an outstanding balance on our revolving credit facility of $17.4 million. The outstanding balance under our revolving credit facility is subject to fluctuating interest rates. A 1% change in the interest rate would yield an additional $174,000 of interest expense. See Note 7 to our consolidated financial statements included in Item 8.

Table of Contents

ITEM 8. ***FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.***

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND RELATED INFORMATION

Reports of Independent Registered Public Accounting Firm Grant Thornton LLP Audited Financial Statements:	37
Consolidated Balance Sheets as of December 31, 2012 and 2011	39
Consolidated Statements of Net Income for the years ended December 31, 2012, 2011 and 2010	40
Consolidated Statements of Shareholders Equity for the years ended December 31, 2012, 2011 and 2010	41
Consolidated Statements of Cash Flows for the years ended December 31, 2012, 2011 and 2010	42
Notes to Consolidated Financial Statements	43

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and

Shareholders of U.S. Physical Therapy, Inc.

We have audited the accompanying consolidated balance sheets of U.S. Physical Therapy, Inc. (a Nevada corporation) and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of net income, shareholders equity and cash flows for each of the three years in the period ended December 31, 2012. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of U.S. Physical Therapy, Inc. and subsidiaries as of December 31, 2012 and 2011, and the results of their consolidated operations and their cash flows for each of the three years in the period ended December 31, 2012 in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), U.S. Physical Therapy, Inc. and subsidiaries internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 12, 2013, expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Houston, Texas

March 12, 2013

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and

Shareholders of U.S. Physical Therapy, Inc.

We have audited U.S. Physical Therapy, Inc. (a Nevada Corporation) and subsidiaries internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). U.S. Physical Therapy, Inc. and subsidiaries management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report appearing under Item 9A on Internal Control over Financial Reporting. Our responsibility is to express an opinion on U.S. Physical Therapy, Inc. and subsidiaries internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, based on our audit, U.S. Physical Therapy, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control Integrated Framework* issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of U.S. Physical Therapy, Inc. and subsidiaries as of December 31, 2012 and 2011, and the related consolidated statements of net income, shareholders equity, and cash flows for each of the three years in the period ended December 31, 2012, and our report dated March 12, 2013 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Houston, Texas

March 12, 2013

Table of Contents

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31, 2012	December 31, 2011
	(In thousands, except per share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 11,671	$ 9,983
Patient accounts receivable, less allowance for doubtful accounts of $1,595 and $2,154, respectively	25,973	28,333
Accounts receivable other, less allowance for doubtful accounts of $514 and $883, respectively	1,703	1,614
Other current assets	5,975	5,737
Total current assets	45,322	45,667
Fixed assets:		
Furniture and equipment	36,316	35,103
Leasehold improvements	20,858	20,385
	57,174	55,488
Less accumulated depreciation and amortization	44,158	42,299
	13,016	13,189
Goodwill	100,188	92,750
Other intangible assets, net	12,146	9,603
Other assets	1,042	2,043
	$ 171,714	$ 163,252
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable trade	$ 1,732	$ 1,809
Accrued expenses	14,116	14,082
Current portion of notes payable	459	433
Total current liabilities	16,307	16,324
Notes payable	175	284
Revolving line of credit	17,400	23,500
Deferred rent	894	941
Other long-term liabilities	2,279	623
Total liabilities	37,055	41,672
Commitments and contingencies		
Shareholders equity:		
U. S. Physical Therapy, Inc. shareholders equity:		
Preferred stock, $.01 par value, 500,000 shares authorized, no shares issued and outstanding		
Common stock, $.01 par value, 20,000,000 shares authorized, 14,129,651 and 13,919,588 shares issued, respectively	141	139
Additional paid-in capital	37,489	36,133
Retained earnings	111,321	102,405
Treasury stock at cost, 2,214,737 shares	(31,628)	(31,628)
Total U. S. Physical Therapy, Inc. shareholders equity	117,323	107,049

Noncontrolling interests	17,336	14,531
Total equity	134,659	121,580
	$ 171,714	$ 163,252

See notes to consolidated financial statements.

Table of Contents

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF NET INCOME

	Year Ended December 31,		
	2012	2011	2010
	(In thousands, except per share data)		
Net patient revenues	$ 244,443	$ 226,579	$ 204,101
Other revenues	7,645	10,427	7,132
Net revenues	252,088	237,006	211,233
Clinic operating costs:			
Salaries and related costs	132,824	125,117	110,872
Rent, clinic supplies, contract labor and other	51,620	47,396	40,944
Provision for doubtful accounts	4,848	3,785	3,241
Closure costs	211	59	163
Total clinic operating costs	189,503	176,357	155,220
Gross margin	62,585	60,649	56,013
Corporate office costs	24,782	24,718	22,823
Operating income	37,803	35,931	33,190
Interest and other income, net	6	5,445	586
Interest expense	(557)	(496)	(236)
Income from operations	37,252	40,880	33,540
Provision for income taxes	11,034	11,097	8,840
Net income including noncontrolling interests	26,218	29,783	24,700
Less: net income attributable to noncontrolling interests	(8,285)	(8,809)	(9,055)
Net income attributable to common shareholders	$ 17,933	$ 20,974	$ 15,645
Earnings per share attributable to common shareholders:			
Basic	$ 1.52	$ 1.78	$ 1.34
Diluted	$ 1.51	$ 1.75	$ 1.32
Shares used in computation:			
Basic	11,804	11,814	11,638
Diluted	11,904	11,977	11,870
Dividends declared per common share	$ 0.76	$ 0.32	$

See notes to consolidated financial statements.

Table of Contents

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

	U. S. Physical Therapy, Inc.								
	Common Stock		Additional		Treasury Stock		Total		
	Shares	Amount	Paid-In Capital	Retained Earnings	Shares	Amount	Shareholders Equity	Noncontrolling Interests	Total
					(In thousands)				
Balance December 31, 2009	13,829	$ 138	$ 43,210	$ 75,632	(2,215)	$ (31,628)	$ 87,352	$ 4,873	$ 92,225
Proceeds from exercise of stock options	68	1	419				420		420
Tax benefit from exercise of stock options			336				336		336
Issuance of restricted stock	93								
Cancellation of restricted stock	(10)								
Compensation expense restricted stock			1,245				1,245		1,245
Compensation expense stock options			47				47		47
Purchase of business								8,133	8,133
Sale of business								(92)	(92)
Acquisition of noncontrolling interests			313				313	37	350
Purchase and retirement of treasury stock	(87)			(1,401)			(1,401)		(1,401)
Distributions to noncontrolling interest partners								(9,580)	(9,580)
Net income				15,645			15,645	9,055	24,700
Balance December 31, 2010	13,893	$ 139	$ 45,570	$ 89,876	(2,215)	$ (31,628)	$ 103,957	$ 12,426	$ 116,383
Proceeds from exercise of stock options	139								
Net tax benefit from exercise of stock options			217				217		217
Issuance of restricted stock	160								
Cancellation of restricted stock	(18)								
Compensation expense restricted stock			2,032				2,032		2,032
Transfer of compensation liability for certain stock issued pursuant to long-term incentive plans			199				199		199
Purchase of business								8,096	8,096
Acquisition of noncontrolling interests			(11,885)				(11,885)	(1,198)	(13,083)
Settlement of purchase price								(3,835)	(3,835)
Purchase and retirement of treasury stock	(255)			(4,656)			(4,656)		(4,656)
Distributions to noncontrolling interest partners								(9,767)	(9,767)
Cash dividends to shareholders				(3,789)			(3,789)		(3,789)
Net income				20,974			20,974	8,809	29,783
Balance December 31, 2011	13,919	$ 139	$ 36,133	$ 102,405	(2,215)	$ (31,628)	$ 107,049	$ 14,531	$ 121,580
Proceeds from exercise of stock options	130	2	20				22		22
Net tax benefit from exercise of stock options			1,209				1,209		1,209
Issuance of restricted stock	81								
Compensation expense restricted stock			2,102				2,102		2,102
Transfer of compensation liability for certain stock issued pursuant to long-term incentive plans			135				135		135
Purchase of business								2,892	2,892
Acquisitions and sales of noncontrolling interests, net			(955)				(955)	(244)	(1,199)
Contribution of noncontrolling interest partners								49	49
			(1,155)				(1,155)	1,155	

Transfer of losses from noncontrolling interests									
Distributions to noncontrolling interest partners								(9,332)	(9,332)
Cash dividends to shareholders				(9,017)			(9,017)		(9,017)
Net income				17,933			17,933	8,285	26,218
Balance December 31, 2012	14,130	$ 141	$ 37,489	$ 111,321	(2,215)	$ (31,628)	$ 117,323	$ 17,336	$ 134,659

See notes to consolidated financial statements.

Table of Contents

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2012	2011	2010
		(In thousands)	
OPERATING ACTIVITIES			
Net income including noncontrolling interests	$ 26,218	$ 29,783	$ 24,700
Adjustments to reconcile net income including noncontrolling interests to net cash provided by operating activities:			
Depreciation and amortization	5,287	5,449	5,667
Provision for doubtful accounts	4,848	3,785	3,241
Gain on purchase price settlement		(5,435)	
Equity-based awards compensation expense	2,102	2,032	1,292
Loss (gain) on sale of business and fixed assets	175	182	(333)
Excess tax benefit from exercise of stock options	1,351	(217)	(336)
Deferred income tax	3,738	3,833	452
Other		437	(414)
Changes in operating assets and liabilities:			
Increase in patient accounts receivable	(1,663)	(5,147)	(4,169)
Increase in accounts receivable other	(561)	(990)	(297)
(Increase) decrease in other assets	(585)	(1,972)	206
(Decrease) increase in accounts payable and accrued expenses	(340)	1,190	(292)
(Decrease) increase in other liabilities	(1,321)	(275)	804
Net cash provided by operating activities	39,249	32,655	30,521
INVESTING ACTIVITIES			
Purchase of fixed assets	(4,234)	(3,222)	(3,673)
Purchase of businesses, net of cash acquired	(7,929)	(9,451)	(18,197)
Acquisitions of noncontrolling interests	(2,244)	(20,439)	(682)
Sale of noncontrolling interests	239		
Settlement of purchase price		1,500	
Proceeds on sale of business and fixed assets, net	64	6	919
Net cash used in investing activities	(14,104)	(31,606)	(21,633)
FINANCING ACTIVITIES			
Distributions to noncontrolling interests	(9,332)	(9,767)	(9,580)
Cash dividends to shareholders	(9,017)	(3,789)	
Purchase and retire of common stock		(4,656)	(1,401)
Proceeds from revolving line of credit	79,900	118,900	46,300
Payments on revolving line of credit	(86,000)	(100,900)	(41,200)
Payment of notes payable	(434)	(250)	(1,013)
Tax benefit from stock options exercised	1,351	217	336
Other	75		420
Net cash used in financing activities	(23,457)	(245)	(6,138)
Net increase in cash and cash equivalents	1,688	804	2,750
Cash and cash equivalents beginning of period	9,983	9,179	6,429
Cash and cash equivalents end of period	$ 11,671	$ 9,983	$ 9,179

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION			
Cash paid during the period for:			
Income taxes	$ 6,361	$ 9,037	$ 7,804
Interest	$ 639	$ 325	$ 179
Non-cash investing and financing transactions during the period:			
Purchase of business seller financing portion	$ 350	$ 200	$ 525
Acquisition of noncontrolling interest seller financing portion	$	$ 367	$

See notes to consolidated financial statements.

Table of Contents

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2012

1. Organization, Nature of Operations and Basis of Presentation

U.S. Physical Therapy, Inc. and its subsidiaries (the Company) operate outpatient physical therapy clinics that provide pre-and post-operative care and treatment for orthopedic-related disorders, sports-related injuries, preventative care, rehabilitation of injured workers and neurological-related injuries. As of December 31, 2012 the Company owned and operated 431 clinics in 43 states including the physician services facility described below. The clinics business primarily originates from physician referrals. The principal sources of payment for the clinics services are managed care programs, commercial health insurance, Medicare/Medicaid, workers compensation insurance and proceeds from personal injury cases. In addition to the Company s ownership of outpatient physical therapy clinics, it also operates a physician services facility which provides services related to intra articular joint and lumbar osteoarthritis programs as well as electro-diagnostic analysis and manages physical therapy facilities for third parties, primarily physicians, with 15 such third-party facilities under management as of December 31, 2012.

The consolidated financial statements include the accounts of U.S. Physical Therapy, Inc. and its subsidiaries. All significant intercompany transactions and balances have been eliminated. The Company primarily operates through subsidiary clinic partnerships in which the Company generally owns a 1% general partnership interest and a 64% limited partnership interest. The managing therapist of each clinic owns the remaining limited partnership interest in the majority of the clinics (hereinafter referred to as Clinic Partnership). To a lesser extent, the Company operates some clinics through wholly-owned subsidiaries under profit sharing arrangements with therapists (hereinafter referred to as Wholly-Owned Facilities).

During the last three years, the Company completed the following multi-clinic acquisitions:

Acquisition	Date	% Interest Acquired	Number of Clinics
	2012		
May 2012 Acquisition	May 22	70%	7
	2011		
July 2011 Acquisition	July 25	51%	20
	2010		
February 2010 Acquisition	February 26	70%	5
December 21, 2010 Acquisition	December 21	70%	6
December 31, 2010 Acquisition	December 31	65%	14

In addition to the 7 clinics in the May 2012 Acquisition, in 2012, the Company acquired 7 clinic practices in 7 separate transactions. Two of the acquired clinic practices will operate in two separate partnerships and the remaining 5 will operate as satellites of existing partnerships. In 2010, the Company acquired two clinic practices in separate transactions. Both practices were consolidated into existing Company clinics.

Clinic Partnerships

For Clinic Partnerships, the earnings and liabilities attributable to the noncontrolling interest, typically owned by the managing therapist, directly or indirectly, are recorded within the statements of net income and balance sheets as noncontrolling interests.

Wholly-Owned Facilities

For Wholly-Owned Facilities with profit sharing arrangements, an appropriate accrual is recorded for the amount of profit sharing due the clinic partners/directors. The amount is expensed as compensation and included

43

Table of Contents

in clinic operating costs salaries and related costs. The respective liability is included in current liabilities accrued expenses on the balance sheet.

Physician Services Revenues

Revenues from physician services are generated by franchisee arrangements with third parties, pursuant to which there are multiple deliverables training and ongoing services as well as through a physician services facility. Each component can be purchased separately. Revenue is recognized over the period the respective services are provided. Physician service revenue are included in other revenues in the accompanying Consolidated Statements of Net Income.

Management Contract Revenues

Management contract revenues are derived from contractual arrangements whereby the Company manages a clinic for third party owners. The Company does not have any ownership interest in these clinics. Typically, revenues are determined based on the number of visits conducted at the clinic and recognized when services are performed. Costs, typically salaries for the Company s employees, are recorded when incurred. Management contract revenues are included in other revenues in the accompanying Consolidated Statements of Net Income.

2. Significant Accounting Policies

Cash Equivalents

The Company maintains its cash and cash equivalents at financial institutions. The combined account balances at several institutions typically exceed Federal Deposit Insurance Corporation (FDIC) insurance coverage and, as a result, there is a concentration of credit risk related to amounts on deposit in excess of FDIC insurance coverage. Management believes that this risk is not significant.

Long-Lived Assets

Fixed assets are stated at cost. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets. Estimated useful lives for furniture and equipment range from three to eight years and for software purchased from three to seven years. Leasehold improvements are amortized over the shorter of the related lease term or estimated useful lives of the assets, which is generally three to five years.

Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

The Company reviews property and equipment and intangible assets with finite lives for impairment upon the occurrence of certain events or circumstances that indicate the related amounts may be impaired. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Goodwill

Goodwill represents the excess of the amount paid and fair value of the non-controlling interests over the fair value of the acquired business assets, which include certain intangible assets. Historically, goodwill has been derived from acquisitions and, prior to 2009, from the purchase of some or all of a particular local management s equity interest in an existing clinic. Effective January 1, 2009, if the purchase price of a non-controlling interest by the Company exceeds or is less than the book value at the time of purchase, any excess or shortfall is recognized as an adjustment to additional paid-in capital.

The fair value of goodwill and other intangible assets with indefinite lives are tested for impairment annually and upon the occurrence of certain events, and are written down to fair value if considered impaired.

Table of Contents

The Company evaluates goodwill for impairment on at least an annual basis (in its third quarter) by comparing the fair value of its reporting units to the carrying value of each reporting unit including related goodwill. The Company operates a one segment business which is made up of various clinics within partnerships. The partnerships are components of regions and are aggregated to the operating segment level for the purpose of determining the Company s reporting units when performing its annual goodwill impairment test.

An impairment loss generally would be recognized when the carrying amount of the net assets of a reporting unit, inclusive of goodwill and other intangible assets, exceeds the estimated fair value of the reporting unit. The estimated fair value of a reporting unit is determined using two factors: (i) earnings prior to taxes, depreciation and amortization for the reporting unit multiplied by a price/earnings ratio used in the industry and (ii) a discounted cash flow analysis. A weight is assigned to each factor and the sum of each weight times the factor is considered the estimated fair value. For 2012, the factors (i.e., price/earnings ratio, discount rate and residual capitalization rate) were updated to reflect current market conditions. The evaluation of goodwill in 2012, 2011 and 2010 did not result in any goodwill amounts that were deemed impaired.

The Company has not identified any triggering events occurring after the testing date that would impact the impairment testing results obtained. Factors which could result in future impairment charges include but are not limited to:

- revenue and earnings expectations;
- general economic conditions;
- regulatory conditions including federal and state regulations;
- changes as the result of government enacted national healthcare reform;
- availability and cost of qualified physical therapists;
- personnel productivity;
- changes in Medicare guidelines and reimbursement or failure of our clinics to maintain their Medicare certification status;
- competitive, economic or reimbursement conditions in our markets which may require us to reorganize or close certain clinics and thereby incur losses and/or closure costs;
- changes in reimbursement rates or payment methods from third party payors including government agencies and deductibles and co-pays owed by patients;
- maintaining adequate internal controls;
- availability, terms, and use of capital;

acquisitions and the successful integration of the operations of the acquired businesses; and

weather and other seasonal factors.

The Company will continue to monitor for any triggering events or other indicators of impairment.

Noncontrolling Interests

The Company recognizes noncontrolling interests as equity in the consolidated financial statements separate from the parent entity s equity. The amount of net income attributable to noncontrolling interests is included in consolidated net income on the face of the income statement. Changes in a parent entity s ownership interest in a subsidiary that do not result in deconsolidation are treated as equity transactions if the parent entity retains its controlling financial interest. The Company recognizes a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss is measured using the fair value of the noncontrolling equity investment on the deconsolidation date.

Table of Contents

When the purchase price of a noncontrolling interest by the Company exceeds the book value at the time of purchase, any excess or shortfall is recognized as an adjustment to additional paid-in capital. Additionally, operating losses are allocated to noncontrolling interests even when such allocation creates a deficit balance for the noncontrolling interest partner.

Revenue Recognition

Revenues are recognized in the period in which services are rendered. Net patient revenues (patient revenues less estimated contractual adjustments) are reported at the estimated net realizable amounts from third-party payors, patients and others for services rendered. The Company has agreements with third-party payors that provide for payments to the Company at amounts different from its established rates. The allowance for estimated contractual adjustments is based on terms of payor contracts and historical collection and write-off experience.

The Company determines allowances for doubtful accounts based on the specific agings and payor classifications at each clinic. The provision for doubtful accounts is included in clinic operating costs in the statement of net income. Net accounts receivable, which are stated at the historical carrying amount net of contractual allowances, write-offs and allowance for doubtful accounts, includes only those amounts the Company estimates to be collectible.

The Medicare program reimburses outpatient rehabilitation providers based on the Medicare Physician Fee Schedule (MPFS). The MPFS rates are automatically updated annually based on a formula, called the sustainable growth rate (SGR) formula. The use of the SGR formula has resulted in calculated automatic reductions in rates in every year since 2002; however, for each year through 2013, Centers for Medicare & Medicaid Services (CMS) or Congress has taken action to prevent the implementation of SGR formula reductions. For 2012, the Temporary Payroll Tax Cut Continuation Act of 2011 (TPTC) delayed application of the SGR for the first two months of the year and the Middle Class Tax Relief and Job Creation Act of 2012 (MCTRA) included a measure freezing payment rates at their then current level through December 31, 2012. The American Taxpayer Relief Act of 2012 essentially froze the Medicare physician fee schedule rates at 2012 levels through December 31, 2013, averting a scheduled 26.5% cut as a result of the SGR formula that would have taken effect on January 1, 2013. A reduction in the Medicare physician fee schedule payment rates will occur on January 1, 2014, unless Congress again takes legislative action to prevent the SGR formula reductions from going into effect.

The Budget Control Act of 2011 increased the federal debt ceiling in connection with deficit reductions over the next ten years, and requires automatic reductions in federal spending by approximately $1.2 trillion. Payments to Medicare providers are subject to these automatic spending reductions, subject to a 2% cap. The American Taxpayer Relief Act of 2012 temporarily delayed the automatic, across-the-board sequestration cuts in federal spending imposed by the Budget Control Act of 2011. Unless further legislation is enacted, it is likely that there will be a 2% reduction to Medicare payments for services furnished on or after April 1, 2013.

The MCTRA directed CMS to implement a claims-based data collection program to gather additional data on patient function during the course of therapy in order to better understand patient conditions and outcomes. All practice settings that provide outpatient therapy services would be required to include this data on the claim form. Beginning on July 1, 2013, therapists will be required to report new codes and modifiers on the claim form that reflect a patient s functional limitations and goals at initial evaluation, periodically throughout care, and at discharge. For claims submitted after July 1, 2013, CMS will reject claims if the required data is not included in the claim.

As a result of the Balanced Budget Act of 1997, the formula for determining the total amount paid by Medicare in any one year for outpatient physical therapy, occupational therapy, and/or speech-language pathology services provided to any Medicare beneficiary (*i.e.*, the Therapy Cap or Limit) was established.

Table of Contents

Based on the statutory definitions which constrained how the Therapy Cap would be applied, there is one Limit for Physical Therapy and Speech Language Pathology Services combined, and one Limit for Occupational Therapy. During 2012, the annual Limit on outpatient therapy services was $1,880 for physical therapy and speech language pathology services combined and $1,880 for occupational therapy services. Pursuant to the final MPFS rule for 2013, effective January 1, 2013 the annual Limit on outpatient therapy services is $1,900 for physical therapy and speech language pathology services combined and $1,900 for occupational therapy services. Historically, these Therapy Caps applied to outpatient therapy services provided in all settings, except for services provided in departments of hospitals. However, the American Taxpayer Relief Act of 2012 extended the annual limits on therapy expenses to services furnished in hospital outpatient department settings from October 1, 2012 through December 31, 2013. Unless Congress enacts legislation to extend the application of these limits to therapy provided in hospital outpatient settings, the Therapy Cap will no longer apply to such services starting as of January 1, 2014.

In the Deficit Reduction Act of 2005, Congress implemented an exceptions process to the annual Limit for therapy expenses. Under this process, a Medicare enrollee (or person acting on behalf of the Medicare enrollee) is able to request an exception from the Therapy Caps if the provision of therapy services was deemed to be medically necessary. Therapy Cap exceptions have been available automatically for certain conditions and on a case-by-case basis upon submission of documentation of medical necessity. The MCTRA extended the exceptions process for outpatient Therapy Caps through December 31, 2012. The American Taxpayer Relief Act of 2012 extended the exceptions process for outpatient Therapy Caps through December 31, 2013. Unless Congress extends the exceptions process, the Therapy Caps will apply to all outpatient therapy services beginning January 1, 2014, except those services furnished and billed by outpatient hospital departments.

Furthermore, under the MCTRA, starting on October 1, 2012, patients who meet or exceed $3,700 in therapy expenditures during a calendar year are subject to a manual medical review prior to payment. The $3,700 threshold is applied to the combined physical therapy/speech language pathology cap; a separate $3,700 threshold is applied to the occupational therapy cap. The American Taxpayer Relief Act of 2012 extends through December 31, 2013 the requirement that Medicare perform manual medical review of therapy services beyond the $3,700 threshold and continued the process by which providers may seek pre-approval for services to be performed beyond such dollar threshold. In February 2013, CMS advised providers that the pre-approval process for services beyond the $3,700 cap will no longer be in effect, so that all such services during the calendar year that are over the dollar threshold will be subject to a manual medical review.

CMS adopted a multiple procedure payment reduction (MPPR) for therapy services in the final update to the MPFS for calendar year 2011. During 2011, the MPPR applied to all outpatient therapy services paid under Medicare Part B occupational therapy, physical therapy and speech-language pathology. Under the policy, the Medicare program pays 100% of the practice expense component of the Relative Value Unit (RVU) for the therapy procedure with the highest practice expense RVU, then reduces the payment for the practice expense component for the second and subsequent therapy procedures or units of service furnished during the same day for the same patient, regardless of whether those therapy services are furnished in separate sessions. In 2011 and 2012 the second and subsequent therapy service furnished during the same day for the same patient was reduced by 20% in office and other non-institutional settings and by 25% in institutional settings. The American Taxpayer Relief Act of 2012 increases the payment reduction to 50%, on subsequent therapy procedures in either setting, effective April 1, 2013. This reduction in payment for our services provided to Medicare beneficiaries will negatively impact the Company s financial results, estimated to represent an 8% to 10% reduction in overall reimbursement for services the Company provides to Medicare beneficiaries.

Statutes, regulations, and payment rules governing the delivery of therapy services to Medicare beneficiaries are complex and subject to interpretation. The Company believes that it is in compliance in all material respects with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing that would have a material effect on the Company s financial statements as of December 31, 2012. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare program.

Table of Contents

Physician Services Revenues

Revenues from physician services are generated by franchisee arrangements with third parties, pursuant to which there are multiple deliverables training and ongoing services as well as through a physician services facility. Each component can be purchased separately. Revenue is recognized over the period the respective services are provided. Physician service revenues are included in other revenues in the accompanying Consolidated Statements of Net Income.

Management Contract Revenues

Management contract revenues are derived from contractual arrangements whereby the Company manages a clinic for third party owners. The Company does not have any ownership interest in these clinics. Typically, revenues are determined based on the number of visits conducted at the clinic and recognized when services are performed. Costs, typically salaries for the Company s employees, are recorded when incurred. Management contract revenues are included in other revenues in the accompanying Consolidated Statements of Net Income.

Contractual Allowances

Contractual allowances result from the differences between the rates charged for services performed and expected reimbursements by both insurance companies and government sponsored healthcare programs for such services. Medicare regulations and the various third party payors and managed care contracts are often complex and may include multiple reimbursement mechanisms payable for the services provided in Company clinics. The Company estimates contractual allowances based on its interpretation of the applicable regulations, payor contracts and historical calculations. Each month the Company estimates its contractual allowance for each clinic based on payor contracts and the historical collection experience of the clinic and applies an appropriate contractual allowance reserve percentage to the gross accounts receivable balances for each payor of the clinic. Based on the Company s historical experience, calculating the contractual allowance reserve percentage at the payor level is sufficient to allow the Company to provide the necessary detail and accuracy with its collectibility estimates. However, the services authorized and provided and related reimbursement are subject to interpretation that could result in payments that differ from the Company s estimates. Payor terms are periodically revised necessitating continual review and assessment of the estimates made by management. The Company s billing system does not capture the exact change in its contractual allowance reserve estimate from period to period in order to assess the accuracy of its revenues and hence its contractual allowance reserves. Management regularly compares its cash collections to corresponding net revenues measured both in the aggregate and on a clinic-by-clinic basis. In the aggregate, historically the difference between net revenues and corresponding cash collections has generally reflected a difference within approximately 1% of net revenues. Additionally, analysis of subsequent period s contractual write-offs on a payor basis reflects a difference within approximately 1% between the actual aggregate contractual reserve percentage as compared to the estimated contractual allowance reserve percentage associated with the same period end balance. As a result, the Company believes that a change in the contractual allowance reserve estimate would not likely be more than 1% at December 31, 2012.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions

Table of Contents

meeting the more-likely-than-not threshold, the amount to be recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

The Company did not have any accrued interest or penalties associated with any unrecognized tax benefits nor was any interest expense recognized during the twelve months ended December 31, 2012 and 2011. The Company will book any interest or penalties, if required, in interest and/or other income/expense as appropriate.

Fair Values of Financial Instruments

The carrying amounts reported in the balance sheet for cash and cash equivalents, accounts receivable, accounts payable and notes payable approximate their fair values due to the short-term maturity of these financial instruments. The carrying amount of the revolving credit facility approximates its fair value. The interest rate on the revolving credit facility, which is tied to the Eurodollar Rate, is set at various short-term intervals, as detailed in the credit agreement.

Segment Reporting

Operating segments are components of an enterprise for which separate financial information is available that is evaluated regularly by chief operating decision makers in deciding how to allocate resources and in assessing performance. The Company identifies operating segments based on management responsibility and believes it meets the criteria for aggregating its operating segments into a single reporting segment.

Use of Estimates

In preparing the Company s consolidated financial statements, management makes certain estimates and assumptions, especially in relation to, but not limited to, goodwill impairment, allowance for receivables, tax provision and contractual allowances, that affect the amounts reported in the consolidated financial statements and related disclosures. Actual results may differ from these estimates.

Self-Insurance Program

The Company utilizes a self insurance plan for its employee group health insurance coverage administered by a third party. Predetermined loss limits have been arranged with the insurance company to minimize the Company s maximum liability and cash outlay. Accrued expenses include the estimated incurred but unreported costs to settle unpaid claims and estimated future claims. Management believes that the current accrued amounts are sufficient to pay claims arising from self insurance claims incurred through December 31, 2012.

Stock Options

The Company measures and recognizes compensation expense for all stock-based payments at fair value. Compensation cost recognized includes compensation for all stock-based payments granted prior to, but not yet vested on January 1, 2006, based on the grant-date fair value estimated at the time of grant and compensation cost for the stock-based payments granted subsequent to January 1, 2006, based on the grant-date fair value. There was no stock option compensation in the years ended December 31, 2012 and 2011. No stock options were granted during the years ended December 31, 2012, 2011 and 2010. As of December 31, 2012, there were no nonvested stock options.

Restricted Stock

Restricted stock issued to employees and directors is subject to continued employment or continued service on the board, respectively. Typically, the transfer restrictions for shares granted to employees lapse in equal installments on the following four or five annual anniversaries of the date of grant. Compensation expense for

Table of Contents

grants of restricted stock is recognized based on the fair value per share on the date of grant amortized over the vesting period. The restricted stock issued is included in basic and diluted shares for the earnings per share computation.

Subsequent Event

The Company has evaluated events occurring after the balance sheet date for possible disclosure as a subsequent event through the date that these financial statements were issued.

3. Acquisitions and Divestiture

Acquisition of Businesses

During 2012, 2011 and 2010, the Company completed the following multi-clinic acquisitions of physical therapy practices:

Acquisition	Date	% Interest Acquired	Number of Clinics
	2012		
May 2012 Acquisition	May 22	70%	7
	2011		
July 2011 Acquisition	July 25	51%	20
	2010		
February 2010 Acquisition	February 26	70%	5
December 21, 2010 Acquisition	December 21	70%	6
December 31, 2010 Acquisition	December 31	65%	14

In addition to the 7 clinics in the May 2012 Acquisition, in 2012, the Company acquired 7 clinic practices in 7 separate transactions. Two of the clinic practices operate in two new partnerships and the remaining 5 operate as satellites of existing partnerships. In 2010, the Company acquired two clinic practices in separate transactions. Both practices were consolidated into existing Company clinics.

The purchase price for the 70% interest in the May 2012 Acquisition was $6,090,000 in cash and $250,000 in seller notes, that are payable in two principal installments totaling $125,000 each, plus any accrued interest, in May 2013 and 2014. The seller notes accrue interest at 3.25% per annum. For the Company, 70% of the goodwill for the May 2012 Acquisition is tax deductible.

In addition to the above multi-clinic acquisitions, in 2012, the Company, through its subsidiaries, purchased 7 outpatient therapy practices in 7 transactions for aggregate cash consideration of $1,938,000 and, in one transaction, a $100,000 note payable. The purchase prices were allocated $43,000 to current assets, $213,000 to non-current assets, $25,000 to non competition agreements, $57,000 to referral relationships and $1,883,000 to goodwill.

The purchase prices for the acquisitions in 2012 have been preliminarily allocated as follows (in thousands):

Cash paid, net of cash acquired..	$	7,929
Seller notes		350
Total consideration	$	8,279
Estimated fair value of net tangible assets acquired:		
Total current assets	$	363
Total non-current assets		478
Total liabilities		(290)

Net tangible assets acquired	$	551
Referral relationships		57
Non compete		25
Goodwill		10,538
Fair value of noncontrolling interest		(2,892)
	$	8,279

Table of Contents

The purchase price plus the fair value of the noncontrolling interest for the 2012 acquisitions was allocated to the fair value of the assets acquired and liabilities assumed based on the preliminary estimates of the fair values at the acquisition date, with the amount exceeding the estimated fair values being recorded as goodwill. The Company is in the process of completing its formal valuation analysis to identify and determine the fair value of tangible and intangible assets acquired and the liabilities assumed. Thus, the final allocation of the purchase price may differ from the preliminary estimates used at December 31, 2012 based on additional information obtained. Changes in the estimated valuation of the tangible and intangible assets acquired and the completion by the Company of the identification of any unrecorded pre-acquisition contingencies, where the liability is probable and the amount can be reasonably estimated, will likely result in adjustments to goodwill.

The purchase price for the 51% interest in the July 2011 Acquisition was $8,426,000, which consisted of $8,226,000 in cash and a $200,000 seller note, that is payable in two principal installments totaling $100,000 each, plus any accrued interest, in July 2012 and 2013. The seller note accrues interest at 3.25% per annum. For the Company 51% of the goodwill for the July 2011 Acquisition is tax deductible.

The purchase price was allocated as follows (in thousands):

Cash paid, net of cash acquired..	$	7,930
Seller notes		200
Total consideration	$	8,130
Estimated fair value of net tangible assets acquired:		
Total current assets	$	1,341
Total non-current assets		902
Total liabilities		(581)
Net tangible assets acquired	$	1,662
Tradename		1,900
Referral relationships		1,100
Non compete		300
Goodwill		11,263
Fair value of noncontrolling interest		(8,095)
	$	8,130

For the July 2011 Acquisition, the purchase price was allocated to the fair value of the assets acquired including tradename, non compete agreements and referral relationships, and to the liabilities assumed based on estimates of the fair values at the acquisition date, with the amount exceeding the fair value being recorded as goodwill. The values assigned to the referral relationships and non compete agreements are being amortized to expense equally over the respective estimated life of 13 years and six years, respectively. The values assigned to goodwill and tradenames are tested annually for impairment. Approximately $5.8 million of the goodwill is tax deductible.

In April 2012, the Company sold 1% of its interest in the July 2011 Acquisition to the limited partners. The Company now owns a 50% interest in the July 2011 Acquisition, 1% as a general partner and 49% as a limited partner.

The purchase price for the 70% interest acquired in the February 2010 Acquisition was $8.9 million, net of cash acquired, which consisted of $8,718,000 in cash and $200,000 in seller notes. The purchase price for the 70% interest acquired in the December 21, 2010 Acquisition was $4.0 million, net of cash acquired, which consisted of $3,877,000 in cash and $100,000 in a seller note. The purchase price for the 65% interest acquired in the December 31, 2010 Acquisition was $4.5 million, net of cash acquired, which consisted of $4,347,000 in cash and $200,000 in a seller note.

Table of Contents

The purchase prices allocated for the 2010 multi-clinic acquisitions in aggregate were as follows (in thousands):

Cash paid, net of cash acquired..	$	16,942
Seller notes		500
Total consideration	$	17,442
Estimated fair value of net tangible assets acquired:		
Total current assets	$	1,765
Total non-current assets		1,308
Total liabilities		(851)
Net tangible assets acquired		2,222
Referral relationships		1,700
Non compete		480
Tradename		2,700
Goodwill		18,471
Fair value of noncontrolling interest		(8,131)
	$	17,442

In addition to the above multi-clinic acquisitions in 2010, on March 1, 2010, a subsidiary of the Company purchased an outpatient therapy practice for $100,000, which consisted of $75,000 of cash and a payable of $25,000. The purchase price was allocated $30,000 to non-current assets and $70,000 to goodwill. Effective July 1, 2010, a subsidiary of the Company purchased an outpatient therapy practice for $100,000, which consisted of $50,000 cash and a payable of $50,000. The purchase price was allocated $30,000 to non-current assets, $20,000 to non competition agreements and $50,000 to goodwill. Both practices were consolidated into existing Company clinics.

For the 2010 multi-clinic acquisitions, the purchase price was allocated to the fair value of the assets acquired including tradenames, non competition agreements and referral relationships, and to the liabilities assumed based on the estimates of the fair values at the acquisition date, with the amount exceeding the estimated fair values being recorded as goodwill. For the Company, its portion of the goodwill is tax deductible. For the 2010 acquisitions, the value assigned to (i) referral relationships is amortized to expense equally over the respective estimated original life which is 12 years for these acquisitions, (ii) non compete agreements are amortized over five to six years and (iii) goodwill and tradenames are tested at least annually for impairment.

For the 2012, 2011 and 2010 acquisitions, total current assets primarily represent patient accounts receivable of $3.5 million. Total non current assets are fixed assets, primarily equipment, used in the practices.

The consideration paid for each of the acquisitions was derived through arm s length negotiations. Funding for the cash portions was derived from proceeds from the Company s revolving credit facility. The results of operations of the acquisitions have been included in the Company s consolidated financial statements since their respective date of acquisition. Unaudited proforma consolidated financial information for the 2012, 2011 and 2010 acquisitions have not been included as the results, individually and in the aggregate, were not material to current operations.

In November 2011, the Company and the seller of the February 2010 Acquisition reached an agreement regarding an adjustment to purchase price as disclosed above. The Company received $1.5 million cash, the forgiveness of the balance of $0.1 million on the notes payable as well as the 30% partnership interest originally held by the seller which had a book value of $3.8 million.

Table of Contents

Acquisitions of Noncontrolling Interests

In 15 separate transactions during 2012, the Company purchased partnership interests in 15 partnerships. The interests in the partnerships purchased ranged from 10% to 35%. The aggregate of the purchase prices paid was $2.2 million, which included $0.2 million of undistributed earnings. The remaining purchase price of $2.0 million, less future tax benefits of $0.8 million, was recognized as an adjustment to additional paid-in capital. During 2012, the Company sold interests in the range of 0.64% to 1% in three partnerships for an aggregate price of $239,000. This amount less related undistributed earnings of $5,000 was credited to additional paid-in capital.

In six separate transactions during 2011, the Company purchased a total of 22.2% of the 30% non-controlling interest in STAR Physical Therapy, LP, a subsidiary of the Company (STAR). The aggregate purchase price paid for the 22.2% interest was $16.9 million, which included $0.8 million of undistributed earnings. The remaining purchase price of $16.1 million, less future tax benefits of $6.3 million, was recognized as an adjustment to additional paid-in capital. After these transactions, the Company owned 92.2% and the non-controlling interest limited partners in aggregate owned the remaining 7.8% in the partnership. Of the 22.2% aggregate non-controlling interests purchased, 17% was held by Regg Swanson, the Managing Director and a founder of STAR and a member of the Company s Board of Directors (Swanson). The purchase prices were determined based on the contractual terms in the Reorganization of Securities Purchase Agreement dated as of September 6, 2007 among the Company, STAR, the limited partners of STAR and Regg Swanson as Seller Representative and in his individual capacity, which was filed as Exhibit 10.1 to the Company s Current Report on Form 8-K filed with the SEC on September 7, 2007. After the sale of his 17.0% interest, Swanson owned 2.0% of STAR (Swanson Interest).

Effective June 30, 2011, the Company purchased the 35% non-controlling interest in one of its Texas partnerships. The aggregate purchase price for the 35% interest was $3.9 million, of which $3.5 million was paid in cash and $367,272 was paid in the form of a note to the seller, which is payable in two equal annual installments of principal plus any accrued and unpaid interest. Interest accrues at 3.25% per annum. The purchase price included $0.2 million of undistributed earnings and $0.2 million in invested capital. The remaining purchase price of $3.5 million, less future tax benefits of $1.4 million, was recognized as an adjustment to additional paid-in capital. After this transaction, the Company owns 100% of the partnership.

In addition, during 2011, the Company purchased the non-controlling interests of several other partners for $142,000, which included $48,000 of undistributed earnings and sold additional interest to an existing partner for $58,000. The net purchase price of approximately $36,000, less future tax benefits of $23,000, was recognized as an adjustment to additional paid-in capital.

During 2010, the Company purchased noncontrolling interests in nine partnerships for an aggregate purchase price of $682,000. The amount paid plus a net deficit of $37,000 in limited partners equity, less tax benefits of $217,000, was recognized as an adjustment to additional paid-in capital.

The results of operations of the acquired noncontrolling interests are included in the accompanying financial statements from the dates of purchase in the net income attributable to common shareholders.

Divestiture of Business

On March 31, 2010, the Company sold its 51% interest in a joint venture of five Texas clinics for $974,000. The Company recorded a pre-tax gain of $578,000, which is included in other income in the Consolidated Statement of Net Income.

The operating results of these locations were not material to the operations of the Company, and therefore, the operating results of these clinics were not reclassified and reported as discontinued operations. The cash flow impact of these clinics was determined to be immaterial to the Consolidated Statements of Cash Flows.

Table of Contents

4. Goodwill

The changes in the carrying amount of goodwill as of December 31, 2012 and 2011 consisted of the following (in thousands):

	Year Ended December 31	
	2012	2011
Beginning balance	$ 92,750	$ 79,424
Goodwill acquired during the year	10,538	15,887
Goodwill allocated to specific assets for businesses acquired in 2011	(3,300)	
Goodwill allocated to specific assets for businesses acquired in 2010		(2,990)
Goodwill adjustments for purchase price allocation of businesses acquired	200	443
Goodwill written off closed clinic		(14)
Ending balance	$ 100,188	$ 92,750

In addition to the goodwill resulting from the 2011 acquisitions, for 2011, the goodwill acquired includes $1.5 million related to additional consideration based on the achievement of operating results for the third year of operations of an acquisition which occurred in 2008. Due to the timing of the acquisition, current accounting regulations required the amounts paid be capitalized as goodwill. These amounts are tax deductible.

5. Intangible Assets, net

Intangible assets, net as of December 31, 2012 and 2011 consisted of the following (in thousands):

	December 31,	
	2012	2011
Tradename	$ 7,973	$ 6,073
Referral relationships, net of accumulated amortization of $1,217 and $784, respectively	3,501	2,777
Non compete agreements, net of accumulated amortization of $1,848 and $1,443, respectively	672	753
	$ 12,146	$ 9,603

Tradenames, referral relationships and non compete agreements are related to the businesses acquired. The value assigned to tradenames has an indefinite life and is tested at least annually for impairment in conjunction with the Company s annual goodwill impairment test. The value assigned to referral relationships is being amortized over their respective estimated useful lives which range from six to 16 years. Non compete agreements are amortized over the respective term of the agreements which range from five to six years.

The following table details the amount of amortization expense recorded for intangible assets for the years ended December 31, 2012, 2011 and 2010 (in thousands):

	Year Ended December 31,		
	2012	2011	2010
Referral relationships	$ 433	$ 305	$ 213
Non compete agreements	405	390	344
	$ 838	$ 695	$ 557

54

Table of Contents

The remaining balance of referral relationships and non compete agreements is expected to be amortized as follows (in thousands):

Referral Relationships		Non Compete Agreements	
Years	Annual Amount	Years	Annual Amount
2013	398	2013	281
2014	395	2014	140
2015	374	2015	140
2016	374	2016	78
2017	374	2017	33
2018	338		
2019	301		
2020	294		
2021	269		
2022	221		
2023	113		
2024	50		

6. Accrued Expenses

Accrued expenses as of December 31, 2012 and 2011 consisted of the following (in thousands):

	Year Ended December 31,	
	2012	2011
Salaries and related costs	$ 8,941	$ 9,275
Group health insurance claims	991	1,168
Credit balances due to patients and payors	813	793
Other	3,371	2,846
Total	$ 14,116	$ 14,082

7. Notes Payable

Notes payable as of December 31, 2012 and 2011 consisted of the following ($ in thousands):

	2012	2011
Revolving credit agreement average effective interest rate of 2.7% inclusive of unused fee	$ 17,400	$ 23,500
Promissory note payable in annual installments of $100 plus accrued interest through December 31, 2012, interest accrues at 3.25% per annum		100
Promissory note payable in annual installments of $50 plus accrued interest through December 21, 2012, interest accrues at 4.00% per annum		50
Promissory note payable in annual installments of $184 plus accrued interest through June 30, 2013, interest accrues at 3.25% per annum	184	367
Promissory note payable in annual installments of $100 plus accrued interest through July 25, 2013, interest accrues at 3.25% per annum	100	200
Promissory note payable in annual installments of $50 plus accrued interest through January 3, 2014, interest accrues at 3.25% per annum	100	
Promissory notes payable in aggregate annual installments of $125 plus accrued interest through May 22, 2014, interest accrues at 3.25% per annum	250	

	18,034	24,217
Less current portion	(459)	(433)
	$ 17,575	$ 23,784

Table of Contents

Effective August 27, 2007, the Company entered into a credit agreement with a commitment for a $30.0 million revolving credit facility which was increased to $50.0 million effective June 4, 2008 (Credit Agreement). Effective March 18, 2009, the Credit Agreement was amended to permit the purchase up to $15,000,000 of the Company s common stock subject to compliance with certain covenants, including the requirement that after giving effect to any stock purchase, the Company s consolidated leverage ratio (as defined in the Credit Agreement) be less than 1.0 to 1.0 and that any stock repurchased be retired within seven days of purchase. Effective October 13, 2010, the Credit Agreement was amended to extend the maturity date from August 31, 2011 to August 31, 2015. In addition, the Credit Agreement was amended to adjust the pricing grid which is based on the Company s consolidated leverage ratio with the applicable spread over LIBOR ranging from 1.6% to 2.5% or the applicable spread over the Base Rate ranging from .1% to 1%. On July 14, 2011, the Credit Agreement was amended to increase the commitment from $50.0 million to $75.0 million. Effective October 24, 2012, the Credit Agreement was amended to permit the Company to purchase, commencing on October 24, 2012 and at all times thereafter, up to $15,000,000 of its common stock subject to compliance with covenants. On December 3, 2012, the Credit Agreement was amended to allow the Company to pay a special dividend of $0.40 per share. The Credit Agreement is unsecured and has loan covenants, including requirements that the Company comply with a consolidated fixed charge coverage ratio and consolidated leverage ratio. Proceeds from the Credit Agreement may be used for working capital, acquisitions, purchases of the Company s common stock, dividend payments to the Company s common stockholders, capital expenditures and other corporate purposes. Fees under the Credit Agreement include an unused commitment fee ranging from .1% to .25% depending on the Company s consolidated leverage ratio and the amount of funds outstanding under the Credit Agreement. On December 31, 2012, $17.4 million was outstanding on the revolving credit facility resulting in $57.6 million of availability. As of December 30, 2012, the Company was in compliance with all of the covenants thereunder.

The Company generally enters into various notes payable as a means of financing a portion of its acquisitions and purchases of non controlling interests. In conjunction with the acquisitions in 2012, the Company entered into notes payable in the aggregate amount of $350,000, each payable in two equal annual installments totaling $175,000 plus any accrued and unpaid interest. Interest accrues at 3.25% per annum.

In conjunction with the July 2011 Acquisition, the Company entered into a note payable in the amount of $200,000 payable in two equal annual installments of $100,000 plus any accrued and unpaid interest. Interest accrues at 3.25% per annum. In June 2011, the Company, in conjunction with the purchase of a non controlling interest, entered into a note payable in the amount of $367,272 payable in two equal annual installments of $183,636 plus any accrued and unpaid interest. Interest accrues at 3.25% per annum.

In conjunction with the 2010 multi-clinic acquisitions, the Company entered into various notes payable aggregating $500,000. The notes were payable in equal annual installments of principal over two years plus any accrued and unpaid interest. Interest accrues at rates ranging from 3.25% to 4.0% per annum. The remaining balance of $100,000 on the notes payable related to the February 2011 Acquisition was forgiven in conjunction with the agreement on the adjustment of the purchase price as disclosed above.

Aggregate annual payments of principal required pursuant to the revolving credit facility and the above notes payable subsequent to December 31, 2012 are as follows (in thousands):

During the twelve months ended December 31, 2013	$ 459
During the twelve months ended December 31, 2014	175
During the twelve months ended December 31, 2015	17,400
	$ 18,034

Table of Contents

8. Income Taxes

Significant components of deferred tax assets included in the consolidated balance sheets at December 31, 2012 and 2011 were as follows (in thousands):

	2012	2011
Deferred tax assets:		
Compensation	$ 1,059	$ 1,253
Allowance for doubtful accounts	607	950
Lease obligations closed clinics	39	139
Depreciation and amortization		58
Other	22	26
Deferred tax assets	$ 1,727	$ 2,426
Deferred tax liabilities:		
Depreciation and amortization	$ (2,166)	$
Other	(575)	(478)
Deferred tax liabilities	(2,741)	$ (478)
Net deferred tax assets (liabilities)	$ (1,014)	$ 1,948
Amount included in:		
Other current assets	$ 590	$ 896
Other assets	$	$ 1,052
Long term liabilities	$ (1,604)	$

During 2012 and 2011, the Company recorded deferred tax assets of $0.8 million and $7.7 million, respectively, related to acquisitions of non controlling interests. At December 31, 2012 and 2011, the Company had a tax receivable of $4.2 million and $3.6 million, respectively, included in other current assets on the accompanying consolidated balance sheets.

The differences between the federal tax rate and the Company s effective tax rate for results of continuing operations for the years ended December 31, 2012, 2011 and 2010 were as follows (in thousands):

	2012		2011		2010	
U. S. tax at statutory rate	$ 10,138	35.0%	$ 11,225	35.0%	$ 8,570	35.0%
State income taxes, net of federal benefit	1,199	4.2%	1,116	3.5%	185	0.7%
Deductible losses	(404)	-1.4%		0.0%		0.0%
Nontaxable gain		0.0%	(1,342)	-4.2%		0.0%
Nondeductible expenses	101	0.3%	98	0.3%	85	0.4%
	$ 11,034	38.1%	$ 11,097	34.6%	$ 8,840	36.1%

Significant components of the provision for income taxes for continuing operations for the years ended December 31, 2012, 2011 and 2010 were as follows (in thousands):

	2012	2011	2010
Current:			
Federal	$ 6,100	$ 5,732	$ 7,730
State	1,196	1,532	658

Total current	7,296	7,264	8,388
Deferred:			
Federal	3,183	3,603	392
State	555	230	60
Total deferred	3,738	3,833	452
Total income tax provision for continuing operations	$ 11,034	$ 11,097	$ 8,840

Table of Contents

During the fourth quarter of 2010, the Company completed a process to perform a detailed reconciliation of its federal and state taxes payable and receivable accounts along with its federal and state deferred tax asset and liability accounts. Historically, calculations of these tax-related accounts were performed through summary estimates and analysis. As a result of this detailed analysis, the Company recorded a reduction in its current state income tax provision of $814,000. The Company considers this reconciliation process to be an annual control and performed a similar reconciliation process during the fourth quarter of 2011 and 2012. For 2011, the adjustment of $162,000 was included in the 2012 state tax provision.

The Company is required to establish a valuation allowance for deferred tax assets if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income in the periods which the deferred tax assets are deductible, management believes that a valuation allowance is not required, as it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets.

The Company s U.S. federal returns remain open to examination for 2009 through 2011 and U.S. state jurisdictions are open for periods ranging from 2008 through 2011.

The Company does not believe that it has any significant uncertain tax positions at December 31, 2012, nor is this expected to change within the next twelve months due to the settlement and expiration of statutes of limitation.

The Company did not have any accrued interest or penalties associated with any unrecognized tax benefits nor was any interest expense recognized during the years ended December 31, 2012 and 2011.

9. Equity Based Plans

The Company has the following equity based plans:

The 1992 Stock Option Plan, as amended (the 1992 Plan), permitted the Company to grant to key employees and outside directors of the Company incentive and non-qualified options to purchase up to 3,495,000 shares of common stock (subject to proportionate adjustments in the event of stock dividends, splits, and similar corporate transactions). The 1992 Plan expired in 2002 and no new option grants can be awarded subsequent to this date. At December 31, 2011 and 2012, there were no stock options outstanding under the 1992 Plan.

Incentive stock options (those intended to satisfy the requirements of the Internal Revenue Code) granted under the 1992 Plan were granted at an exercise price not less than the fair market value of the shares of common stock on the date of grant. The exercise prices of options granted under the 1992 Plan were determined by the Compensation Committee. The period within which each option is exercisable was determined by the Compensation Committee (however, in no event may the exercise period of an incentive stock option extend beyond 10 years from the date of grant).

The Amended and Restated 1999 Employee Stock Option Plan (the Amended 1999 Plan) permits the Company to grant to non-employee directors and employees of the Company up to 600,000 non-qualified options to purchase shares of common stock and restricted stock (subject to proportionate adjustments in the event of stock dividends, splits, and similar corporate transactions). The exercise prices of options granted under the Amended 1999 Plan are determined by the Compensation Committee. The period within which each option will be exercisable is determined by the Compensation Committee. The Amended 1999 Plan was approved by the shareholders of the Company at the 2008 Shareholders Meeting on May 20, 2008.

Table of Contents

During 2003, the Board of Directors of the Company (the Board) granted inducement options covering 145,000 options, respectively, to five individuals in connection with their offers of employment. As of December 31, 2011, 124,000 of the 145,000 options are outstanding. Inducement options may be exercised for a 10 year term from the date of the grant. As of December 31, 2012, there were no stock options outstanding under these inducement options.

The Amended and Restated 2003 Stock Option Plan (the Amended 2003 Plan) permits the Company to grant to key employees and outside directors of the Company incentive and non-qualified options and shares of restricted stock covering up to 1,250,000 shares of common stock (subject to proportionate adjustments in the event of stock dividends, splits, and similar corporate transactions). The Amended 2003 Plan was approved by the shareholders of the Company at the 2010 Shareholders Meeting on May 18, 2010.

A cumulative summary of equity plans as of December 31, 2012 follows:

Equity Plans	Authorized	Restricted Stock Issued	Outstanding Stock Options	Stock Options Exercised	Stock Options Exercisable	Shares Available for Grant
1992 Plan	3,495,000			2,796,012		
Amended 1999 Plan	600,000	360,900	15,840	123,951	15,840	99,309
Amended 2003 Plan	1,250,000	253,400	60,000	718,300	60,000	218,300
Inducements	164,000			164,000		
	5,509,000	614,300	75,840	3,802,263	75,840	317,609

A summary of the status of the Company s stock options granted under the plans as of December 31, 2012, 2011 and 2010 and the changes during the years then ended is presented below:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (000 s)
Outstanding at December 31, 2009	874,192	14.24	4.6 Years	
Granted				
Exercised	(142,002)	13.66		
Cancelled	(160)	18.42		
Forfeited	(8,140)	18.54		
Outstanding at December 31, 2010	723,890	14.30	3.6 Years	
Granted				
Exercised	(375,080)	13.92		
Cancelled				
Forfeited				
Outstanding at December 31, 2011	348,810	14.71	2.6 Years	
Granted				
Exercised	(272,750)	14.12		
Cancelled	(220)	17.89		
Forfeited				
Outstanding at December 31, 2012	75,840		2.2 Years	
Exercisable at December 31, 2012	75,840		2.2 Years	$ 811

All shares pursuant to stock options were fully vested at December 31, 2012 and 2011.

Table of Contents

A summary of the intrinsic value of stock options exercised during the years ended December 31, 2012, 2011 and 2010 is as follows:

	Number of Shares	Aggregate Intrinsic Value (000)
2010	142,002	$ 863
2011	375,080	$ 3,160
2012	272,750	$ 3,459

The following tables summarize information about the Company s stock options outstanding as of December 31, 2012, 2011 and 2010, respectively:

	Outstanding Options as of December 31, 2012	Exercise Price		Weighted Average Remaining Contractual Life	Exercisable	Exercise Price	
1999 Plan	15,840	$ 12.60	$18.42	2.2 Years	15,840	$ 12.60	$18.42
2003 Plan	60,000	$ 12.51	$18.80	2.2 Years	60,000	$ 12.51	$18.80
	75,840	$ 12.51	$18.80	2.2 Years	75,840	$ 12.51	$18.80

	Outstanding Options as of December 31, 2011	Exercise Price		Weighted Average Remaining Contractual Life	Exercisable	Exercise Price	
1999 Plan	17,310	$ 12.60	$18.42	3.2 Years	17,310	$ 12.60	$18.42
2003 Plan	251,500	$ 12.51	$18.80	2.9 Years	251,500	$ 12.51	$18.80
Inducements	80,000	$ 12.75	$14.32	1.7 Years	80,000	$ 12.75	$14.32
	348,810	$ 12.51	$18.80	2.6 Years	348,810	$ 12.51	$18.80

	Outstanding Options as of December 31, 2010	Exercise Price		Weighted Average Remaining Contractual Life	Exercisable	Exercise Price	
1992 Plan	15,000	$	16.34	.6 Years	15,000	$	16.34
1999 Plan	43,390	$ 12.60	$18.42	3.9 Years	43,390	$ 12.60	$18.42
2003 Plan	541,500	$ 12.51	$18.80	3.8 Years	541,500	$ 12.51	$18.80
Inducements	124,000	$ 12.75	$14.32	2.8 Years	124,000	$ 12.75	$14.32
	723,890	$ 12.51	$18.80	3.6 Years	723,890	$ 12.51	$18.80

The following table summarizes information about the Company s stock options outstanding and those options that are exercisable as of December 31, 2012:

Range of Exercise Prices

		Outstanding Options	Exercisable Options
$12.00	$12.99	11,790	11,790
$14.00	$14.99	2,500	2,500
$15.00	$15.99	12,550	12,550
$18.00	$18.80	49,000	49,000
		75,840	75,840

Table of Contents

During 2012, 2011 and 2010, the Company granted the following shares (net of those shares cancelled in their respective grant year due to employee terminations prior to restrictions lapsing) of restricted stock to directors, officers and employees pursuant to its equity plans as follows:

Year Granted	Number of Shares	Weighted Average Fair Value Per Share
2010	84,400	$ 16.53
2011	156,750	$ 19.94
2012	80,650	$ 21.65

Generally, restrictions on the stock granted to employees lapse in equal annual installments on the following four or five anniversaries of the date of grant. For those shares granted to directors, the restrictions will lapse in equal quarterly installments during the first year after the date of grant. For those granted to executive officers, the restriction will lapse in equal quarterly installments during the three to four years following the date of grant.

As of December 31, 2012, there were 187,170 shares outstanding for which restrictions had not lapsed. The restrictions will lapse in 2013 through 2016.

Compensation expense for grants of restricted stock will be recognized based on the fair value on the date of grant. Compensation expense for restricted stock grants was $2,102,000, $2,032,000 and $1,245,000, respectively, for 2012, 2011 and 2010. As of December 31, 2012, the remaining $2.8 million of compensation expense will be recognized from 2013 through 2016.

10. Preferred Stock

The Board is empowered, without approval of the shareholders, to cause shares of preferred stock to be issued in one or more series and to establish the number of shares to be included in each such series and the rights, powers, preferences and limitations of each series. There are no provisions in the Company s Articles of Incorporation specifying the vote required by the holders of preferred stock to take action. All such provisions would be set out in the designation of any series of preferred stock established by the Board. The bylaws of the Company specify that, when a quorum is present at any meeting, the vote of the holders of at least a majority of the outstanding shares entitled to vote who are present, in person or by proxy, shall decide any question brought before the meeting, unless a different vote is required by law or the Company s Articles of Incorporation. Because the Board has the power to establish the preferences and rights of each series, it may afford the holders of any series of preferred stock, preferences, powers, and rights, voting or otherwise, senior to the right of holders of common stock. The issuance of the preferred stock could have the effect of delaying or preventing a change in control of the Company.

11. Common Stock

In September 2001 through December 31, 2008, the Board of Directors (Board) authorized the Company to purchase, in the open market or in privately negotiated transactions, up to 2,250,000 shares of its common stock. However, the terms of the Company s revolving credit facility had prohibited such purchases since August 2007. As of December 31, 2008, there were approximately 50,000 shares remaining that could be purchased under those programs. In March 2009, the Board authorized the repurchase of up to 10% or approximately 1,200,000 shares of its common stock (March 2009 Authorization). In connection with the March 2009 Authorization, the Company amended its revolving credit facility to permit the share repurchases. The Company is required to retire shares purchased under the March 2009 Authorization. Since there is no expiration date for these share repurchase programs, additional shares may be purchased from time to time in the open market or private transactions depending on price, availability and the Company s cash position. The Company did not purchase any shares in 2012. During 2011, the Company purchased 254,642 shares of its common stock for an

Table of Contents

aggregate cost of $4.7 million. During 2010, the Company purchased 86,522 shares for an aggregate purchase price of $1.4 million. There were approximately 390,000 shares remaining that could be purchased under these programs.

12. Defined Contribution Plan

The Company has a 401(k) profit sharing plan covering all employees with three months of service. The Company may make discretionary contributions of up to 50% of employee contributions. The Company did not make any discretionary contributions and recognized no contribution expense for the years ended December 31, 2012, 2011 and 2010.

13. Commitments and Contingencies

Operating Leases

The Company has entered into operating leases for its executive offices and clinic facilities. In connection with these agreements, the Company incurred rent expense of $20.8 million, $19.4 million and $16.8 million for the years ended December 31, 2012, 2011 and 2010, respectively. Several of the leases provide for an annual increase in the rental payment based upon the Consumer Price Index. The majority of the leases provide for renewal periods ranging from one to five years. The agreements to extend the leases specify that rental rates would be adjusted to market rates as of each renewal date.

The future minimum operating lease commitments for each of the next five years and thereafter and in the aggregate as of December 31, 2012 are as follows (in thousands):

2013	$ 16,254
2014	11,900
2015	9,105
2016	5,526
2017	2,915
Thereafter	1,920
	$ 47,620

Employment Agreements

At December 31, 2012, the Company had outstanding employment agreements with three of its executive officers. These agreements, which presently expire on December 31, 2014, provide for automatic one year renewals if not terminated on at least 12 months notice. All of the agreements contain a provision for annual adjustment of salaries.

In addition, the Company has outstanding employment agreements with most of the managing physical therapist partners of the Company s physical therapy clinics and with certain other clinic employees which obligate subsidiaries of the Company to pay compensation of $17.4 million in 2013 and $5.9 million in the aggregate from 2014 through 2017. In addition, most of the employment agreements with the managing physical therapists provide for monthly bonus payments calculated as a percentage of each clinic s net revenues (not in excess of operating profits) or operating profits.

Table of Contents

14. Earnings Per Share

The computations of basic and diluted earnings per share for the years ended December 31, 2012, 2011 and 2010 are as follows (in thousands, except per share data):

	2012	2011	2010
Numerator:			
Net income attributable to common shareholders	$ 17,933	$ 20,974	$ 15,645
Denominator:			
Denominator for basic earnings per share weighted-average shares	11,804	11,814	11,638
Effect of dilutive securities Stock options	100	163	232
Denominator for diluted earnings per share adjusted weighted-average shares and assumed conversions	11,904	11,977	11,870
Earnings per common share:			
Basic net income attributable to common shareholders	$ 1.52	$ 1.78	$ 1.34
Diluted net income attributable to common shareholders	$ 1.51	$ 1.75	$ 1.32

All options to purchase shares for the year ended December 31, 2012 and 2011 were included in the diluted earnings per share calculation as the average market price for 2012 and 2011 exceeded the options exercise price. Options to purchase 92,900 shares for the year ended December 31, 2010 were excluded from the diluted earnings per share calculation for the respective periods because the options exercise prices exceeded the average market price of the common shares during the periods.

15. Selected Quarterly Financial Data (Unaudited)

	2012			
	Q1	Q2	Q3	Q4
	(In thousands, except per share data)			
Net patient revenues	$ 60,499	$ 62,052	$ 60,782	$ 61,110
Net revenues	$ 62,582	$ 63,959	$ 62,853	$ 62,694
Income from operations	$ 9,871	$ 10,598	$ 9,392	$ 7,942
Net income including noncontrolling interests	$ 6,812	$ 7,314	$ 6,298	$ 5,794
Net income attributable to common shareholders	$ 4,478	$ 4,849	$ 4,563	$ 4,043
Earnings per common share:				
Basic net income attributable to common shareholders	$ 0.38	$ 0.41	$ 0.39	$ 0.34
Diluted net income attributable to common shareholders	$ 0.38	$ 0.41	$ 0.38	$ 0.34
Shares used in computation:				
Basic	11,726	11,781	11,827	11,911
Diluted	11,838	11,903	11,928	12,013

	2011			
	Q1	Q2	Q3	Q4
	(In thousands, except per share data)			
Net patient revenues	$ 53,872	$ 56,678	$ 57,332	$ 58,697
Net revenues	$ 56,741	$ 59,912	$ 59,675	$ 60,678
Income from operations	$ 8,611	$ 10,775	$ 8,507	$ 12,987
Net income including noncontrolling interests	$ 6,185	$ 7,603	$ 5,853	$ 10,142
Net income attributable to common shareholders	$ 3,746	$ 4,900	$ 4,099	$ 8,229
Earnings per common share:				

Basic net income attributable to common shareholders	$ 0.32	$ 0.42	$ 0.35	$ 0.70
Diluted net income attributable to common shareholders	$ 0.31	$ 0.41	$ 0.34	$ 0.69
Shares used in computation:				
Basic	11,718	11,807	11,886	11,786
Diluted	11,945	11,999	12,011	11,892

Table of Contents

ITEM 9. ***CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.***
Not applicable.

ITEM 9A. ***CONTROLS AND PROCEDURES.***
Evaluation of Disclosure Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Exchange Act) as of the end of the fiscal period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective in ensuring that the information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure.

Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting during the quarter ended December 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under Exchange Act. U.S. Physical Therapy, Inc and subsidiaries (the Company) internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Internal control over financial reporting includes those policies and procedures that:

- Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of the Company s management and directors; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company s assets that could have a material effect on the financial statements.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, the risk.

Table of Contents

Management conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2012. In making this assessment, management used the criteria described in Internal Control Integrated *Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2012.

The Company s internal control over financial reporting has been audited by Grant Thornton LLP, an independent registered public accounting firm, as stated in their report included on page 38.

ITEM 9B. ***OTHER INFORMATION***

Not applicable.

Table of Contents

PART III

ITEM 10. ***DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.***

The information required in response to this Item 10 is incorporated herein by reference to our definitive proxy statement relating to our 2013 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 11. ***EXECUTIVE COMPENSATION.***

The information required in response to this Item 11 is incorporated herein by reference to our definitive proxy statement relating to our 2013 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 12. ***SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.***

The information required in response to this Item 12 is incorporated herein by reference to our definitive proxy statement relating to our 2013 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 13. ***CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.***

The information required in response to this Item 13 is incorporated herein by reference to our definitive proxy statement relating to our 2013 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 14. ***PRINCIPAL ACCOUNTANT FEES AND SERVICES.***

The information required in response to this Item 14 is incorporated herein by reference to our definitive proxy statement relating to our 2013 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

Table of Contents

PART IV

ITEM 15. ***EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.***

(a) Documents filed as a part of this report:

1. *Financial Statements.* Reference is made to the Index to Financial Statements and Related Information under Item 8 in Part II hereof, where these documents are listed.

2. *Financial Statement Schedules.* See page 73 for Schedule II Valuation and Qualifying Accounts. All other schedules are omitted because of the absence of conditions under which they are required or because the required information is shown in the financial statements or notes thereto.

3. *Exhibits.* The exhibits listed in List of Exhibits on the next page are filed or incorporated by reference as part of this report.

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3.3	Bylaws of the Company, as amended [filed as an exhibit to the Company s Form 10-KSB for the year ended December 31, 1993 and incorporated herein by reference Commission File Number 1-11151].
10.1+	1992 Stock Option Plan, as amended [filed as an exhibit to the Company s Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference].
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10.3+	1999 Employee Stock Option Plan (as amended and restated May 20, 2008) [incorporated by reference to Appendix A to the Company s Definitive Proxy Statement on Schedule 14A, filed with the SEC on April 17, 2008].
10.4+	U. S. Physical Therapy, Inc. 2003 Stock Incentive Plan, as amended and restated March 26, 2010 [incorporated by reference to Appendix A to the Company s proxy statement on Schedule 14A filed with the SEC on April 9, 2010].
10.5+	Non-Statutory Stock Option Agreement dated February 26, 2002 between the Company and Mary Dimick [filed as an exhibit to the Company s Registration Statement on Form S-8 dated February 10, 2003 Reg. No. 333-103057- and incorporated herein by reference].
10.6+	Non-Statutory Stock Option Agreement dated May 20, 2003 between the Company and Jerald Pullins [filed as an exhibit to the Company s Registration Statement on Form S-8 filed March 15, 2004 Reg. No. 333-113592 and incorporated herein by reference].
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Number	Description
10.27	Credit Agreement, dated as of August 27, 2007 among U. S. Physical Therapy, Inc., as the Borrower, Bank of America, N. A., as Administrative Agent, Swing Line Lender and L/C Issuer, and The Other Lenders Party Hereto [incorporated by reference to Exhibit 10.2 to the Company s Current Report on Form 8-K/A filed with the SEC on September 5, 2007].
10.28	First Amendment to Credit Agreement dated as of June 4, 2008 by and among U.S. Physical Therapy, Inc., a Nevada Corporation, the Lenders party hereto, and Bank of America, N. A., as Administrative Agent [incorporated by reference to Exhibit 10.1 to the Company s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2008, filed with the SEC on August 11, 2008].
10.29	Second Amendment to Credit Agreement and Consent by and among the Company and the Lenders party hereto, and Bank of America, N. A., as Administrative Agent (incorporated by reference to Exhibit 99.1 to the Company Current Report on Form 8-K filed with the SEC on March 18, 2010).
10.30	Third Amendment to Credit Agreement dated as of October 13, 2010, by and among the Company and the Lenders party hereto, and Bank of America, N.A. as administrative Agent [incorporated by reference to Exhibit 10.30 to the Company Annual Report on Form 10-K filed with the SEC on March 10, 2011].
10.31+	U. S. Physical Therapy, Inc. Objective Long-Term Incentive Plan for Senior Management, effective March 27, 2012 (incorporated by reference to Exhibit 99.1 to the Company s Current Report on Form 8-K filed with the SEC on March 28, 2012).
10.32+	U. S. Physical Therapy, Inc. Discretionary Long-Term Incentive Plan for Senior Management for 2012, effective March 27, 2012 (incorporated by reference to Exhibit 99.2 to the Company s Current Report on Form 8-K filed with the SEC on March 28, 2012).
10.33+	U. S. Physical Therapy, Inc. Objective Cash Bonus Plan for 2012, effective March 27, 2012 (incorporated by reference to Exhibit 99.3 to the Company s Current Report on Form 8-K filed with the SEC on March 28, 2012).
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10.38	Amendment to employment agreement effective March 8, 2013 between U. S. Physical Therapy, Inc. and Lawrance M. McAfee. *
10.39	Amendment to employment agreement effective March 8, 2013 between U. S. Physical Therapy, Inc. and Glenn D. McDowell. *
21.1*	Subsidiaries of the Registrant
23.1*	Consent of Independent Registered Public Accounting Firm Grant Thornton LLP

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Number	Description
31.1*	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended
31.2*	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended
31.3*	Certification of Controller pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended
32.1*	Certification of Periodic Report of the Chief Executive Officer, Chief Financial Officer and Controller pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

* Filed herewith
\+ Management contract or compensatory plan or arrangement.

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders

U.S. Physical Therapy, Inc.

We have audited in accordance with the standards of the Public Company Accounting Oversight Board (United States) the consolidated financial statements of U.S. Physical Therapy, Inc. (a Nevada Corporation) and subsidiaries (the Company) referred to in our report dated March 12, 2013, which is included in the annual report to security holders and included in Part II of this form. Our audits of the consolidated financial statements included the financial statement schedule listed in the index appearing under item 15, which is the responsibility of the Company s management. In our opinion, this financial statement schedule, when considered in relation to the consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ GRANT THORNTON LLP

Houston, Texas

March 12, 2013

Table of Contents

FINANCIAL STATEMENT SCHEDULE*

SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

COL. A	COL B	COL C Additions		COL D	COL E
Description	Balance at Beginning of Period	Charged to Costs and Expenses	Charged to Other Accounts	Deductions	Balance at End of Period
	(Amounts in Thousands)				
YEAR ENDED DECEMBER 31, 2012:					
Reserves and allowances deducted from asset accounts:					
Allowance for doubtful accounts(1)	$ 3,037	$ 4,848		$ 5,776(2)	$ 2,109
YEAR ENDED DECEMBER 31, 2011:					
Reserves and allowances deducted from asset accounts:					
Allowance for doubtful accounts	$ 2,273	$ 3,785		$ 3,021(2)	$ 3,037
YEAR ENDED DECEMBER 31, 2010:					
Reserves and allowances deducted from asset accounts:					
Allowance for doubtful accounts	$ 1,872	$ 3,241		$ 2,840(2)	$ 2,273

(1) Related to patient accounts receivable and accounts receivable other.
(2) Uncollectible accounts written off, net of recoveries.
* All other schedules are omitted because of the absence of conditions under which they are required or because the required information is shown in the financial statements or notes thereto.

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

U.S. PHYSICAL THERAPY, INC.
(Registrant)

By: /s/ LAWRANCE W. MCAFEE
Lawrance W. McAfee
Chief Financial Officer

By: /s/ JON C. BATES
Jon C. Bates
Vice President/Controller

Date: March 12, 2013

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated as of the date indicated above.

By:	/s/ CHRISTOPHER J. READING **Christopher J. Reading**	President, Chief Executive Officer and Director (principal executive officer)
By:	/s/ LAWRANCE W. MCAFEE **Lawrance W. McAfee**	Executive Vice President, Chief Financial Officer and Director (principal financial and accounting officer)
By:	/s/ JERALD PULLINS **Jerald Pullins**	Chairman of the Board
By:	/s/ DANIEL C. ARNOLD **Daniel C. Arnold**	Vice Chairman of the Board
By:	/s/ MARK J. BROOKNER **Mark J. Brookner**	Director
By:	/s/ HARRY S. CHAPMAN **Harry S. Chapman**	Director
By:	/s/ BERNARD A. HARRIS, JR. **Bernard A. Harris, Jr.**	Director
By:	/s/ MARLIN W. JOHNSTON **Marlin W. Johnston**	Director
By:	/s/ REGG SWANSON **Regg Swanson**	Director

By: /s/ CLAYTON TRIER Director

Clayton Trier

Table of Contents

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